Table 2

Increases in corporate financial assets

average percent shares of total net incremental placements

	1970-74	1975-79	1980-83
By instrument			
Deposits	61.2	40.4	51.1
Yen			
Demand and time	59.0	25.3	7.8
CDs	—	3.9	16.6
Foreign currency	2.2	1.2	26.7
Equity	28.9	29.4	36.5
Other securities	9.9	30.2	12.4
Percent of total			
In foreign currency	2.8	2.7	34.8
Open-market interest-bearing	8.1	31.3	54.1

Table 3

Increases in personal financial assets

average percent shares of total net incremental placements

	1970-74	1975-79	1980-82
Cash and demand deposits	20.0	10.7	5.2
Time and savings deposits	53.0	55.4	56.4
Postal savings	15.5	20.8	22.8
Private institutions	37.5	34.5	33.6
Trust and insurance investments	18.9	20.4	26.6
*Equities**	0.5	0.9	0.6
Central government bonds	0.6	0.4	5.2
Other	7.0	8.5	6.0

*At acquisition cost.

new entrants as long as possible. Given Japan's demographic profile and the projected size of government borrowing, the major growth areas are seen as government bond distribution and dealing, pension fund management, and life insurance.

In the matter of government bond distribution and dealing by entities other than securities companies, the rules have recently been significantly relaxed. Later this year, for example, "qualified" foreign banks can trade existing government bonds for their own account, as designated commercial banks are now beginning to do. This concession to banks is being made primarily to prepare for the quantum jump in government bond issues beginning next year as the large issues of 10-year government bonds that have been offered continuously since 1975 start to mature. The government's gross borrowing requirement will nearly double next year (see Chart 7). The terms on new bonds will have to approximate the prevailing yields in free secondary markets and will add to pressures for interest rate liberalization. Otherwise, regulated institutions may lose market share or even fail.

The growth in pension business involves not only an increase in traditional fund management but also of annuity business. Companies are seeking to lessen strains on their own resources by moving away from the customary lump-sum settlements to retirees (made generally at the age of 55). Besides one city bank operating under a grandfather clause, there are only twenty-one life insurance companies and seven trust banks that can engage in pension business under existing laws. Most major Japanese financial institutions, as well as some foreign institutions, are devoting considerable resources to gear up for entry into this prime growth area.

As restrictions on the size and maturity of negotiable CDs are relaxed, market pressures are building to decontrol rates on regular savings and time deposits, including those on small postal deposits administered by the Postal Ministry. It has been commonly assumed that decontrol of large deposits, those most vulnerable to competition from rival instruments, would precede the freeing of small deposits. However this may not be so, given the tangle of political and bureaucratic vested interests in the status quo and their conflicting objectives for the future. No matter that there are official proponents of deregulation, resolution of differences will be slow at best.

It is unclear whether deposit rate deregulation will result in generally higher lending rates to ultimate borrowers. Even if deposit rates rise, financial intermediaries should have scope to cut back noninterest expenses. Further, to the extent the relatively free rates in negotiable CD and repo markets already determine the marginal cost of funds, lending rates could be little affected.

As deposit rates are freed, pressures for lending rate liberalization will also mount. The traditional mechanism — the prime rate system — adjusts loan rates in lockstep with the official discount rate and the yield on long-term credit bank debentures. In turn, the latter is linked to the new-issue rate on long-term government bonds. This mechanism is outdated and is seen by Japanese bankers as a competitive handicap. As a test case, they are planning to offer yen loans to high-grade foreign borrowers at rates linked to those on CDs. Such a loan rate would be 7.5%, well below the 7.9% conventional long-term prime rate but close to the 7.3%-7.4% on yen bonds issued by foreign borrowers. With the prospect for greater fluctuation in both deposit and lending rates, the lending

Chart 6

Interest rates and inflation

in percent

of long-term funds at fixed rates will likely decline, challenging the continuing distinction between institutions specializing in short- and long-term finance.

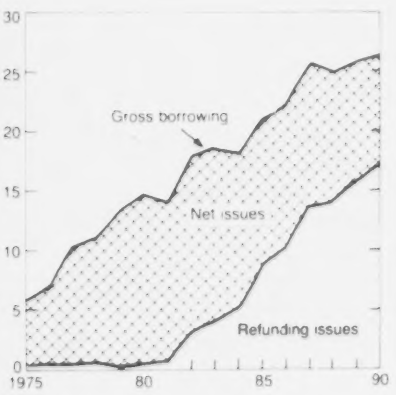
Market segmentation also will erode as the various institutions compete with the new financial products made possible by rapidly changing information technology. For example, it is probable that securities companies will soon introduce cash-management services. As U.S. experience makes clear, these are functionally indistinguishable from the transactions services provided by commercial banks. For the securities companies this innovation represents a quid pro quo for the commercial banks' entry into government bond dealing.

Financial innovations and disparate institutional interests are moving the Japanese financial system inexorably toward greater deregulation and competition, despite the continuing official concern to safeguard institutions that would lose from a financial free-for-all and to manage any adverse consequences thereof.

Chart 7

Government borrowing

official projections for central government bond issues, in trillions of yen



Internationalization of the yen and Japan's global integration

The post-oil shock environment also created pressures on Japan for *external* financial liberalization. When the country's current account balance turned temporarily into deficit, controls on capital inflows were relaxed to help finance increased oil costs. After December 1973 residents were permitted to issue foreign-currency denominated bonds. Such issues had been banned during the previous three years when the current account had been in surplus and the yen was under strong upward pressure. There also was easing of controls on inflows of portfolio and direct investment, motivated partly by reciprocity considerations that were forcefully advanced by Japan's trade partners. In May 1979 the prohibition on foreign participation in the expanding repo market was repealed. Foreign investors were allowed full participation in the CD issue and secondary markets that opened in the same year. However, cumbersome prenotification and re-registration requirements in the secondary market frustrated foreign investors.

The slowing of Japan's own economic growth after the oil shock heightened the interest of Japanese firms in expanding operations abroad, pulling in their wake Japanese banks, which also were hit by the slowdown at home. Japanese companies sought both to increase their investment returns and to diversify their assets. More generally, the question was how best to deploy Japan's excess domestic savings. At least for a time, the authorities endeavored to manage these pressures for internationalization with a deliberate eye to their exchange rate objectives, easing — and, sometimes, reimposing — controls on foreign exchange transactions to influence the yen's value against other currencies.

Many liberalization steps were at first informal, such as the 1979 relaxation of maturity and eligibility restrictions on impact loans to include general trading companies as borrowers and foreign subsidiaries of Japanese banks as lenders. Other important elements of liberalization were formally ratified or introduced by the 1980 overhaul of Japan's exchange control law.

In contrast to the earlier predisposition toward prohibition, the revised principle was that external transactions should be free. Nonetheless, an elaborate system for monitoring capital inflows and outflows was retained, important discretionary controls remained in place, and the murky application of

Table 4

Domestic and Eurocurrency capital markets: end-1983

data partly estimated from 1982 outstandings and 1983 transactions; in billions of dollars, except as noted

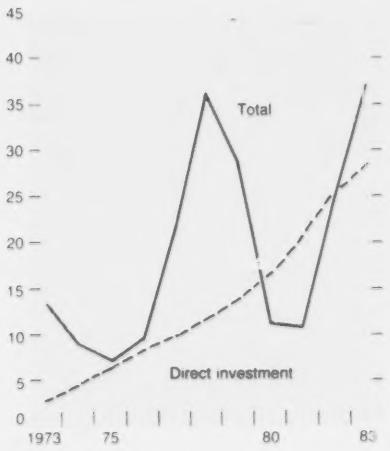
	Japan	United States	Germany
Direct investment assets	33	213	30
as % of 1983 GNP	2.8	6.4	4.5
Direct investment liabilities	4	112	19
as % of 1983 GNP	0.4	3.4	3.0
Domestic equities and bonds	1434	4104	451
of which foreign-held	80	263	22
foreign-held as % of total	5.5	6.4	4.8
as % of 1983 GNP	6.9	7.9	3.3
Foreign bonds issued in domestic market	14.4	63.5	16.5*
Foreign holdings of short-term local currency bank liabilities	13.7	138.9**	17.5
of which, deposits	9.5	36.3**	n.a.
Eurobonds***	1.4	113.4	16.5*
Eurocurrency deposits***	34	1722	181

*Distribution of DM bonds estimated from new issue volume since 1976.
**In currencies of respective countries.
***IBF liabilities classified in Eurodollar deposits.

Chart 8

Net external asset position

in billions of dollars



administrative guidance continued. Besides, "emergency" provisions enabled the authorities in effect to suspend the new law's application in the event of balance of payments deterioration, large fluctuations in the yen or other currencies, or large transfers of funds between Japan and other countries adversely affecting domestic money and capital markets.

The revised law mainly affected four classes of international transactions. First, instead of the earlier Y3 million limit, Japanese residents were granted unlimited freedom to exchange yen into foreign currency deposits. Second, Japanese banks were permitted to borrow and lend foreign currencies without restriction at home and abroad, at least in principle; the remaining restrictions on their granting of impact loans also were lifted. Third, Japanese companies were given greater freedom to borrow abroad. Fourth, the scope for foreign investment in Japanese securities was materially widened, especially in equities. For example, the former general limitation of foreign ownership to 25% was lifted, except for a select list of "designated" companies, 11 in number. However, the government has retained discretion to amend that list.

Cumulatively, Japan's gradual relaxation of external controls has led to significant integration of its capital markets with those abroad, although that integration is by no means complete. The legacy of past restrictions shows in direct investment, where Japan's net position has grown year after year (see Chart 8). Despite Japan's higher economic growth performance and potential, cumulative foreign direct investment in Japan is the lowest among major industrial countries relative to GNP (see Table 4).

In the area of portfolio investment, by contrast, global integration of Japan's capital market has proceeded rapidly of late. By 1982 only U.S. stock and bond markets outranked Japan's in foreign participation, both absolutely and relative to market capitalization and GNP. Moreover, Japan is now second only to the United States as an issuing center for foreign bonds (local-currency-denominated international bonds issued by foreigners) (see Chart 9).

In other respects, however, internationalization of the yen is barely off the ground. The yen shares of both Eurocurrency deposits and Eurobond markets remain negligible, principally because the Japanese authorities are reluctant to see the offshore yen market grow. They fear erosion of their ability to maintain domestic monetary control. For the same reason, Japan has discouraged the yen's potential reserve currency function. At the end of 1982, only 3.7% of world official foreign exchange reserves were held in yen — barely one-third the proportion held in German marks (see Table 5). Euroyen restrictions and the absence of a treasury bill market are the main impediments to the yen's assumption of a reserve role commensurate with Japan's economic power.

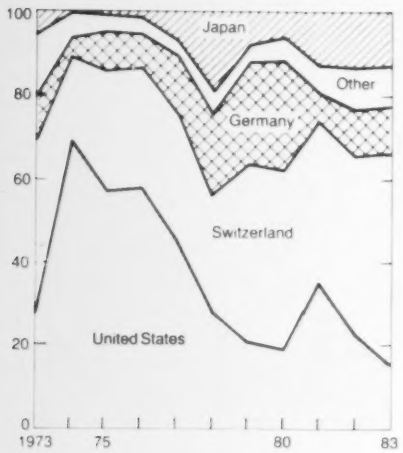
Further evidence of the yen's limited internationalization can be seen in its modest use in trade finance. Without even touching its potential application in third-country trade, the yen at present is used to denominate only some 40% of Japan's own exports. Of Japanese imports, a mere 3% are yen-based — a condition said to reflect dollar pricing in the markets for the fuel and raw materials that make up virtually all of Japan's merchandise imports. One deterrent to a more significant role for the yen in trade finance would seem to be the absence of a yen bankers' acceptance market.

Since the mid-1960s Japan has recorded net long-term capital outflows in every year save 1980, out-

Chart 9

New foreign bond issues by market

percent shares



flows that have accelerated since 1981 in response to high U.S. interest rates and the December 1980 relaxation of capital controls. Significantly, the widening of net capital outflows from Japan has been due solely to the surge in gross capital *outflows*. Gross capital *inflows* have remained essentially steady (see Chart 10). The contrast between vigorous outflows and sluggish inflows gives some credence to foreign suspicions that Japan has managed its external liberalization in a way that depresses the yen's exchange value and thereby maintains unfair competitive advantage for Japanese business. The Japanese, however, maintain that it is high U.S. interest rates that are the prime cause of the capital flow imbalance.

U.S.-Japan joint initiatives

By the time of President Reagan's visit to Japan last November, the United States was convinced that yen undervaluation could not be remedied without tackling Japan's Byzantine system of financial regulation. This has restricted the range of attractive yen assets, has impeded use of the yen as a major international vehicle and reserve currency, and has limited trade in financial services where U.S. institutions enjoy comparative advantage. Accordingly, the United States has pressed manifold proposals to open up the Euroyen market, to further liberalize Japan's domestic financial system, and to improve opportunities for foreign financial institutions in Japan.

Last November, the U.S. and Japanese governments reached an eight-point agreement by which the Japanese Ministry of Finance committed itself to ease guidelines on Euroyen bond issuance by residents; to reform the designated company system; to relax size and maturity restrictions on CDs; and to submit a bill enabling the issue of foreign-currency, government-guaranteed "Nakasone" bonds. In principle, these measures should help strengthen the yen by encouraging capital inflows into Japan. There was a further commitment to eliminate the "real demand" rule governing forward foreign exchange transactions, a rule hindering cross-currency hedging and swaps.

These commitments have since been implemented, at least to a degree. But their practical consequences may not be great unless the new freedoms are actively exploited — which is by no means certain. For example, on April 1 the number of Japanese firms eligible to issue Euroyen bonds, straight or convertible, was increased considerably. However, since such Euroyen issues by residents are subject to withholding taxes, there is more active interest in the functionally similar, but tax-exempt, yen-linked Eurodollar bonds and also in low-coupon convertibles.

Along with the November agreement, the U.S. and Japanese governments formed a joint working group to develop recommendations for further reforms. In April, during these discussions, quotas on medium- and long-term yen bank lending abroad were abolished. But the Ministry of Finance has strengthened reporting requirements, which would facilitate restrictions in the event such lending shows "unusual" increase.

As the discussions of the working group progressed, the proposed timing of future decontrol measures was made known. Starting this month, for example, both Japanese and non-Japanese banks are allowed to make short-term Euroyen loans; yen bond market restrictions are being eased to accommodate additional foreign private borrowers besides the official issuers who have predominated to date; qualified domestic banks may undertake second-

Table 5

The yen as reserve currency

percent shares of world official foreign exchange reserves; year-end data

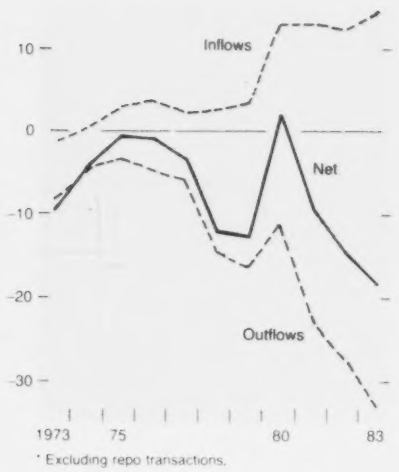
	1975	1980	1982
Japanese yen	0.6	3.2	3.7
Dollar	85.1	59.2	63.5
European currency unit	0.0	17.9	15.3
German mark	6.6	12.5	11.0
Swiss franc	1.7	2.8	2.5
Pound sterling	4.1	2.6	2.1
Other	1.9	1.0	1.9

*French franc and Dutch guilder. Reserve holdings of unknown currency composition are omitted from the share calculations.

Chart 10

Long-term capital flows *

in billions of dollars



* Excluding repo transactions.

ary dealing in gc nds; and currency s ts ol- ished for all ban . rther reforms, to take effect by December, will permit issuance and trading of Euroyen CDs with up to six-month maturities, virtually eliminate ceilings on Euroyen bond issues by nonresidents, and allow foreign institutions to lead-manage Euroyen bond issues.

With these plans disclosed in advance, the May 29 final report of the working group introduced only three new decisions of real significance: from April 1985 banks will be allowed to issue new types of large denomination deposit instruments at market interest rates; interest rate controls on large time deposits are to be abolished or substantially relaxed within two to three years; and foreign banks will be allowed to enter domestic trust and pension business within one year, possibly through wholly owned subsidiaries or by joint ventures with Japanese trust banks.

Assessment

Both governments hailed the agreements reached by the working group as a "historic document." Indeed, the collective breadth and depth of the liberalization measures introduced or planned since last November surpass most early hopes. The new opportunities accorded foreign financial institutions are encouraging, as exemplified by the abolition of swap limits and the commitment to grant trust licenses to foreign banks. More important, and in the face of muted opposition from the Bank of Japan and the strong resistance of long-term credit banks, the Euroyen market is being effectively opened except for two remaining restrictions: the withholding tax levied on interest received by nonresident holders of Euroyen bonds issued by residents; and, with the apparent exception of Euroyen lending by non-Japanese banks to nonresidents, the prohibition of syndicated Euroyen loans with maturities beyond one year. While troublesome, these restrictions should not stifle many dimensions of potential growth in Euroyen business. Its growth will spur domestic liberalization.

Nevertheless, major tasks still lie ahead. Several critical issues have been deferred for further study or lack official commitment to definite action: abolition of the above-noted withholding tax; establishment of a yen bankers' acceptance market, likely to be resolved by the end of this year; establishment of markets for currency futures and treasury bills; decontrol of rates on small deposits, to be achieved only over some unspecified, longer time period because of the postal savings problem; and regular foreign membership in the Tokyo Stock Exchange, which restricts the number of seats to a mere 83 at a going price of Y1 billion ($4 million).

Besides, many features of the working group agreement, such as those that provide a role in implementation for advisory committees, fall short of watertight commitment on the part of the Japanese authorities. Thus follow-through is all-important, especially in view of the long history of problems with Japan's lack of administrative transparency, at least in the eyes of foreign institutions.

Moreover, despite the major concessions toward fostering Euroyen markets, there is continuing official ambivalence toward an international role for the yen commensurate with Japan's economic size, partly out of ostensible concern for effective monetary control. This concern underlies the reluctance to set up an offshore market in Tokyo akin to New York's IBFs. Monetary control could be adversely affected if residents' and nonresidents' demand

Table 6

Increases in corporate liabilities and stock issue

average percent shares of total net incremental finance

	1970-74	1978-80	1981-83
By source			
Loans	83.9	58.1	60.9
Yen	82.5	53.2	47.7
Foreign currency	1.4	4.8	13.2
Bonds	6.0	17.1	14.1
Yen	6.1	13.0	4.6
Foreign currency	—0.1	4.1	9.5
Stocks	10.1	24.9	25.0
Domestic issue	10.1	24.1	23.4
Foreign issue	0.0	0.8	1.6
By currency			
Yen	98.7	90.3	75.8
Foreign currency	1.3	9.7	24.2

proves unpredictable, either for the money stock in Japan or its monetary base. In fact, both the money multiplier linkage between the monetary base and the aggregates and the income velocity linkage of the aggregates to nominal spending appear relatively stable. Further, U.S. evidence suggests monetary base control need not be endangered by offshore markets, provided exchange and interest rates are allowed to fluctuate freely. Thus, Japan's concern may be exaggerated.

It is vital that the free world's second largest economy be integrated into the global financial system. Not only does this promise economic benefits for Japan, especially for its own consumers of financial services, it also can help defuse some of the resentment felt by its trade partners who believe Japan still is unwilling to accept the international responsibility that comes with economic power. If it is true that Japan enjoys an enduring comparative advantage in manufacturing, it follows that others have a comparative advantage in the field of financial and other services. Bringing down the barriers to trade in services would be mutually beneficial.

It is wise not to expect too much from the new U.S.-Japanese agreement in the way of yen appreciation. Simultaneous two-way liberalization of capital inflows and outflows may not secure predictable strengthening of the currency in the short run, as is evident from recent experience with the liberalization of the portfolio rules for Japanese insurers. Their buildup of foreign assets has undoubtedly depressed the yen, given the large interest rate differential in favor of the dollar. How soon that diversification drive will be satisfied is difficult to judge. In the longer run, however, thoroughgoing two-way liberalization, emphasizing introduction of a broad menu of yen assets accessible and attractive to foreigners, should shift portfolio preferences and may well lead to a new capital-flow equilibrium in which the yen strengthens.

There is another way in which the new agreement may help create a more level playing field for Japan's competitors. Historically, high savings in Japan, together with a debt-oriented financing structure and artificially low interest rates in a sheltered environment, provided Japanese industry a major advantage in its effective cost of capital. That advantage has eroded significantly, given the rise in Japan's interest rates and its industry's increased resort both to equity and to foreign bond and loan finance (see Table 6). Closer integration of Japanese and global capital markets should further narrow the remaining capital cost advantage.

However, Japan's liberalization and integration commitments have to be translated into practice. External political considerations now make it imperative that Japan be seen to proceed expeditiously and wholeheartedly with the implementation of its agreement with the United States. Indeed, Japan's trade partners would be further encouraged in their hopes that Japan is now fully committed to a liberal financial order, if Japan were to accelerate its timetable for decontrol and adopt additional liberalization measures, many of which already command significant acceptance in principle.

In addition, basic economic policy changes are needed. Japan's partners — especially the United States and the EC — should recognize that their trade differences with Japan, while sometimes stemming from unequal competitive conditions, more often reflect their own deficient savings and laggardly restructuring by their own industries. Often, their savings are hampered by lax budget policies and fiscal disincentives. By contrast, Japan has consistently encouraged high personal savings through tax and institutional incentives. On both sides, the time is overdue for greater convergence of saving. So long as Japan saves more domestically than it invests at home, current account surpluses and companion trade problems are likely to persist.

Statistical appendix

for key to data in tables see April 1984 issue.

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Information herein is from sources considered to be reliable but is furnished without responsibility on the part of Morgan Guaranty Trust Company.

Nominal effective exchange rates

Index numbers, 1980-82 average = 100. Each index shows a currency's trade-weighted appreciation or depreciation measured against 15 other major currencies, using averages of daily noon spot exchange rates in New York and bilateral trade weights based on 1980 trade in manufactures. Annual figures are calendar year averages.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Netherlands	Spain	Switzerland	Denmark	Norway	Sweden
Pre-June 1970 parities	114.6	114.4	69.0	116.4	111.1	66.2	226.2	147.5	80.6	91.1	82.1	143.2	51.3	113.0	92.3	119.6
Smithsonian central rates	103.1	121.9	77.2	116.7	109.8	68.9	220.9	146.7	80.6	92.3	82.9	142.7	53.2	110.8	90.9	117.6
1980	90.7	100.4	95.5	96.0	106.5	100.0	108.4	99.8	99.4	105.9	100.2	106.5	95.4	105.1	98.2	103.9
1981	99.5	100.2	105.8	104.0	100.4	97.2	98.8	102.1	98.9	101.8	97.1	99.4	98.3	99.2	100.1	103.3
1982	109.8	99.4	98.6	100.1	93.1	102.8	92.8	98.1	101.7	92.3	102.7	94.1	106.3	95.7	101.7	92.8
1983	114.2	100.8	107.8	92.0	87.3	107.6	90.3	91.6	103.6	90.0	105.0	78.4	111.5	96.4	99.4	82.2
1983																
June	114.3	100.8	106.6	89.4	86.4	107.6	90.7	93.6	103.4	90.2	104.6	78.3	110.6	96.2	99.5	82.2
July	115.1	101.0	106.9	89.8	86.2	107.2	90.6	93.4	103.5	89.7	104.5	76.8	111.7	95.4	99.9	82.6
August	117.0	101.2	106.2	91.5	85.6	106.5	89.6	94.0	103.1	89.2	104.1	77.0	112.3	94.5	100.3	82.8
September	116.7	101.3	107.1	92.2	85.6	106.9	88.9	93.8	103.3	88.8	104.2	76.7	112.4	94.9	100.9	82.6
October	114.8	101.0	110.7	93.5	85.4	108.0	88.6	92.2	103.8	88.7	105.0	76.0	113.2	95.2	100.8	82.3
November	116.5	100.9	110.7	94.8	85.1	107.1	88.3	92.8	103.2	88.4	104.4	75.9	112.8	94.6	100.9	82.7
December	118.0	100.4	112.1	94.2	84.7	106.8	88.0	91.8	102.8	88.2	104.1	75.8	113.8	94.0	99.5	83.1
1984																
January	119.1	100.5	113.3	95.5	84.1	106.5	87.6	91.5	102.6	87.7	103.7	76.3	113.8	93.6	99.2	83.4
February	117.3	100.2	111.9	97.3	84.7	108.0	87.0	91.4	103.5	88.3	104.3	77.1	112.2	94.0	99.0	82.9
March	115.4	98.0	114.7	97.2	85.3	109.0	87.2	89.8	104.2	89.0	105.0	77.2	111.7	94.6	98.7	83.5
April	116.7	97.5	115.7	95.1	85.2	108.6	87.3	88.9	104.1	89.0	104.8	78.1	111.3	94.0	98.9	83.7
May	119.4	96.8	114.6	95.1	84.6	107.7	87.0	89.3	103.7	88.8	104.4	78.4	110.8	93.6	99.1	83.5
May 4	118.3	97.0	115.9	96.3	84.8	107.9	86.8	89.4	103.8	88.7	104.3	78.3	110.9	93.6	99.2	83.7
11	119.7	96.8	115.5	95.6	84.4	107.4	86.8	89.5	103.5	88.7	104.3	78.3	110.8	93.4	99.2	83.6
18	119.7	96.9	114.0	94.3	84.5	107.6	87.0	89.5	103.8	88.8	104.4	78.5	110.8	93.7	98.9	83.6
25	119.7	96.7	113.8	94.6	84.5	107.9	87.1	89.0	103.7	89.0	104.5	78.5	110.8	93.6	99.0	83.5
June 1	119.2	96.8	114.0	94.1	84.9	108.2	87.0	88.9	103.8	88.8	104.5	78.2	110.9	93.6	99.1	83.3

Real effective exchange rates

Index numbers, 1980-82 average = 100. Each index is the corresponding nominal effective exchange rate adjusted for differential inflation in wholesale prices of nonfood manufactures. Underlying price data are partly estimated. Index revisions reflect revised price information or, less frequently, adoption of new price indices to measure inflation in one or more countries.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Netherlands	Spain	Switzerland	Denmark	Norway	Sweden
1980	89.5	99.6	103.1	93.0	102.2	103.5	103.5	99.3	100.2	107.5	100.0	102.0	98.7	103.7	96.7	101.3
1981	100.7	100.0	104.7	102.8	100.2	97.4	98.7	102.1	99.1	100.3	97.7	99.0	98.8	99.4	101.0	102.1
1982	109.8	100.4	92.3	104.2	97.7	99.1	97.8	98.6	100.7	92.2	102.4	99.0	102.5	97.0	102.4	96.6
1983	112.6	103.0	96.5	99.9	95.9	99.3	100.0	93.0	101.6	91.9	101.7	89.5	105.2	98.6	101.1	91.4
1983																
June	112.7	103.4	95.4	96.8	94.4	99.4	100.2	95.2	101.1	92.5	101.1	89.6	104.2	99.0	101.5	91.1
July	113.4	103.7	95.3	97.4	95.2	98.5	100.3	94.9	101.3	91.9	101.4	87.8	104.9	96.9	101.0	92.7
August	115.4	103.9	93.7	99.6	94.5	98.1	99.0	95.4	100.6	91.6	101.0	88.0	105.9	96.2	101.0	93.1
September	114.1	104.4	94.8	100.9	95.1	98.3	99.5	95.4	100.6	90.7	101.0	88.3	105.6	97.7	103.2	92.4
October	113.2	103.2	97.3	102.2	95.5	98.9	99.6	93.5	101.4	90.6	100.9	87.8	105.8	97.6	102.6	92.4
November	114.4	103.2	97.3	104.0	95.5	97.8	99.6	94.3	100.8	90.5	100.2	88.3	105.8	96.8	102.3	93.2
December	115.4	102.9	98.5	103.6	95.5	97.3	99.7	93.0	100.4	90.5	99.7	88.8	106.3	95.6	101.3	94.0
1984																
January	116.1	103.4	99.1	105.2	94.3	96.7	100.2	92.9	102.1	89.4	100.6	89.8	106.0	95.3	101.2	95.0
February	114.1	103.4	97.6	107.4	95.7	97.8	100.0	92.9	102.9	89.4	101.0	90.9	104.2	96.9	101.4	94.6
March	112.0	101.4	99.8	107.5	96.8	98.4	100.4	91.5	103.6	90.1	101.8	91.6	103.6	96.2	100.8	95.7
April	113.0	101.1	100.4	105.3	96.7	97.8	101.2	90.7	103.0	89.8	102.0	93.1	103.0	95.1	100.6	96.5
May	115.3	100.7	99.1	105.5	96.4	96.8	101.4	91.2	103.0	89.3	101.9	94.0	102.3	94.7	100.9	96.7

Eurocurrency deposit rates

prime banks' bid rates, at or near end of month

		1980	1981	1982	1983		1984				
		Dec	Dec	Dec	Nov	Dec	Jan	Feb	Mar	Apr	May
Eurodollar	*overnight*	19.25	12.87	9.25	9.00	9.50	9.25	9.38	10.13	10.25	**10.50**
	one month	19.12	13.31	9.12	9.69	9.69	9.50	9.88	10.44	10.63	**11.06**
	three months	17.55	13.75	9.19	9.75	9.81	9.63	10.13	10.63	10.94	**11.75**
	six months	16.37	14.81	9.50	9.94	10.06	9.88	10.38	10.94	11.25	**12.50**
	twelve months	14.87	14.75	9.62	10.31	10.37	10.19	10.81	11.44	11.75	**13.63**
Euro-Canadian dollar	*one month*	17.50	15.37	10.00	9.25	9.12	9.63	9.63	10.00	10.00	**10.69**
	three months	16.88	15.37	10.00	9.37	9.50	9.63	9.81	10.38	10.50	**11.38**
	six months	15.37	16.37	10.13	9.56	9.75	9.88	10.00	10.69	10.94	**12.31**
	twelve months	14.00	16.37	10.25	9.75	10.00	10.06	10.38	11.19	11.44	**13.38**
Euro-French franc	*one month*	11.12	15.75	23.00	12.25	12.12	12.13	16.00	12.94	11.94	**12.00**
	three months	11.75	17.00	24.00	13.19	12.19	13.00	17.25	14.38	13.13	**13.18**
	six months	12.25	18.00	22.00	14.12	12.31	13.75	16.75	15.13	13.88	**14.18**
	twelve months	12.87	18.25	19.75	14.69	12.62	14.38	16.13	15.88	14.88	**14.94**
Euromark	*one month*	8.87	10.44	5.87	6.19	5.25	5.69	5.69	5.50	5.44	**5.63**
	three months	8.87	10.50	5.87	6.19	5.87	5.88	5.81	5.56	5.63	**5.94**
	six months	8.87	10.56	5.94	6.19	6.12	6.19	6.94	5.75	5.75	**6.25**
	twelve months	8.93	10.25	6.00	6.44	6.37	6.38	6.19	6.13	6.19	**6.81**
Euro-Dutch guilder	*one month*	8.87	10.75	5.12	6.00	5.81	5.88	5.94	6.06	5.75	**5.94**
	three months	9.31	10.75	5.19	6.19	6.00	5.94	6.00	6.06	5.94	**6.13**
	six months	9.37	10.75	5.38	6.31	6.25	6.13	6.06	6.19	6.06	**6.44**
	twelve months	9.62	10.75	5.63	6.62	6.37	6.44	6.44	6.50	6.44	**6.94**
Euro-Swiss franc	*one month*	6.00	8.87	2.81	4.06	3.37	3.00	3.44	3.50	3.31	**3.94**
	three months	6.00	9.25	3.25	4.06	3.75	3.44	3.63	3.63	3.63	**4.06**
	six months	5.75	9.25	3.44	4.19	3.94	3.81	3.88	3.81	3.94	**4.44**
	twelve months	5.50	8.50	3.44	4.37	3.94	3.94	4.13	4.13	4.19	**4.75**
Eurosterling	*one month*	14.75	15.37	10.56	9.06	9.12	9.19	9.13	8.75	8.56	**8.94**
	three months	14.75	15.69	10.44	9.25	9.31	9.38	9.19	8.88	8.81	**9.81**
	six months	14.25	15.69	10.31	9.44	9.50	9.56	9.31	9.06	9.06	**10.44**
	twelve months	14.00	15.37	10.31	9.69	9.81	9.88	9.50	9.31	9.38	**10.94**
Euroyen	*one month*	9.12	6.12	6.75	7.25	6.25	6.13	6.88	6.19	6.00	**6.38**
	three months	9.25	6.12	6.75	6.75	6.31	6.31	6.56	6.19	6.19	**6.38**
	six months	9.62	6.87	7.10	6.69	6.38	6.31	6.50	6.25	6.25	**6.44**
	twelve months	9.37	6.87	6.81	6.69	6.44	6.44	6.63	6.38	6.31	**6.56**
European currency unit	*one month*	11.04	14.63	12.44	8.44	8.63	8.81	9.00	10.00	8.81	**9.00**
	three months	11.57	14.75	12.31	8.81	9.06	9.19	9.31	10.00	9.06	**9.38**
	six months	11.75	15.00	12.00	9.19	9.44	9.44	9.63	10.00	9.56	**9.88**
	twelve months	11.65	14.56	11.19	9.63	9.63	9.63	9.94	10.13	10.00	**10.25**

International bond issues — by currency

new issues with a maturity of three years or more, publicly offered or privately placed in the period
millions of dollars

	1981	1982	1983	1984			Jan-May	
				Mar	Apr	May	1984	1983
Eurobonds	**31 616**	**51 645**	**48 476**	**5 988**	**6 114**	**1 391**	**28 697**	**20 666**
U.S. dollar	26 830	43 959	38 403	4 139	4 871	1 119	22 602	16 648
Canadian dollar	634	1 201	1 039	111	106	10	355	416
German mark	1 277	2 588	3 817	406	466	91	1 832	2 130
British pound	501	748	1 947	623	270	—	1 715	395
Japanese yen	368	374	212	—	133	65	305	148
European composite units	309	1 980	2 019	491	123	80	1 295	577
Other	1 697	795	1 039	218	145	26	593	352
Foreign bonds	**21 369**	**26 397**	**26 822**	**2 841**	**4 083**	**1 495**	**13 282**	**13 716**
U.S. dollar	7 552	5 946	4 545	1 078	1 690	150	3 218	2 498
German mark	1 310	2 952	2 671	154	132	146	901	1 347
Dutch guilder	481	956	1 053	—	67	65	352	593
British pound	746	1 214	811	51	184	126	628	169
Swiss franc	8 285	11 432	14 299	1 287	1 649	572	6 390	7 123
Japanese yen	2 457	3 418	3 772	266	356	303	1 438	1 730
Other	538	479	671	5	5	133	355	256
Total	**52 985**	**78 042**	**76 298**	**8 829**	**10 197**	**2 886**	**41 979**	**34 382**

International bond issues — by country of borrower

new issues with a maturity of three years or more, publicly offered or privately placed in the period
millions of dollars

	1981	1982	1983	1984			Jan-May	
				Mar	Apr	May	1984	1983
Industrial countries	**40 861**	**63 062**	**60 278**	**8 096**	**8 995**	**2 506**	**36 606**	**28 874**
Australia	991	2 250	2 529	271	171	98	870	525
Austria	1 557	1 668	1 265	261	235	50	1 045	765
Belgium	527	211	1 153	161	146	43	350	404
Canada	10 648	11 979	7 411	568	1 091	164	3 256	3 722
Denmark	695	1 269	1 719	384	130	100	1 487	626
Finland	672	815	866	185	80	102	702	460
France	3 156	8 456	6 461	375	5	285	2 591	3 872
Germany	279	1 101	3 095	140	18	—	912	1 637
Ireland	517	625	959	73	—	55	227	251
Italy	1 108	2 214	1 565	250	20	60	662	331
Japan	6 928	8 397	13 966	1 357	2 322	906	8 750	7 173
Netherlands	630	894	946	98	150	—	645	284
New Zealand	1 107	1 375	560	—	247	65	443	448
Norway	530	832	699	77	100	65	367	268
Portugal	30	206	76	100	—	60	181	46
South Africa	92	374	548	168	69	101	434	298
Spain	444	747	1 470	251	135	—	702	518
Sweden	2 050	2 479	3 812	1 261	1 644	99	3 725	2 080
United Kingdom	1 408	1 201	1 398	333	390	—	1 886	634
United States	6 770	14 538	7 486	1 377	1 956	153	6 448	3 211
*Other**	722	1 431	2 294	406	86	100	923	1 321
Developing countries	**4 886**	**5 003**	**2 535**	**110**	**95**	**151**	**974**	**600**
Latin American countries	**3 658**	**2 480**	**71**	—	—	**21**	**21**	**21**
Argentina	195	—	—	—	—	—	—	—
Brazil	60	91	—	—	—	—	—	—
Chile	30	—	—	—	—	—	—	—
Colombia	20	35	—	—	—	—	—	—
Mexico	3 012	1 919	—	—	—	—	—	—
Panama	25	—	21	—	—	—	—	21
Venezuela	291	385	—	—	—	—	—	—
*Other***	—	50	50	—	—	21	21	—
Asian countries	**1 068**	**2 075**	**2 252**	**110**	**95**	**130**	**913**	**579**
Hong Kong	70	40	50	—	—	—	—	—
India	271	225	60	50	—	25	75	40
Indonesia	97	412	328	—	—	20	20	37
Korea	323	172	556	60	45	50	250	244
Malaysia	—	807	883	—	—	35	385	201
Philippines	99	50	—	—	—	—	—	—
Singapore	30	125	70	—	—	—	—	—
Thailand	93	63	265	—	50	—	183	17
Other	85	181	40	—	—	—	—	40
Middle Eastern and African countries	**160**	**448**	**212**	—	—	—	**40**	—
Egypt	—	75	—	—	—	—	40	—
Israel	117	200	135	—	—	—	—	—
United Arab Emirates	—	20	—	—	—	—	—	—
Other	43	153	77	—	—	—	—	—
Centrally planned countries	**75**	**65**	**75**	—	—	—	—	**25**
China	—	65	50	—	—	—	—	—
Hungary	20	—	—	—	—	—	—	—
*Other****	55	—	25	—	—	—	—	25
International organizations***	**7 163**	**9 912**	**13 410**	**623**	**1 107**	**229**	**4 359**	**4 883**
Total	**52 985**	**78 042**	**76 298**	**8 829**	**10 197**	**2 886**	**41 979**	**34 382**

*Includes multinational organizations. **Includes unallocated. ***Includes COMECON institutions. ****Includes regional development organizations.

International bond yields

average yield of several actively traded, high quality issues with a maturity of 7 to 12 years
at or near end of month

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States companies											
Eurodollar	n.a.	n.a.	11.16	11.13	11.29	11.41	11.59	11.43	11.77	12.28	12.53
Euromark	n.a.	n.a.	7.24	7.35	7.23	7.23	7.34	7.34	7.26	7.24	7.29
Swiss franc	n.a.	n.a.	5.61	5.78	5.75	5.73	5.73	5.58	5.61	5.63	5.59
European governments											
Eurodollar	n.a.	n.a.	12.53	12.40	12.44	12.52	12.65	12.33	12.58	12.96	13.27
Euromark	n.a.	n.a.	8.10	8.18	8.05	8.07	8.12	8.08	7.63	7.82	7.88
Swiss franc	n.a.	n.a.	5.36	5.61	5.52	5.52	5.59	5.43	5.33	5.34	5.35
European currency unit	n.a.	n.a.	n.a.	11.57	11.64	11.75	11.77	11.53	11.08	11.29	11.44

Eurocurrency bank credits — by country of borrower

credits with a maturity of one year or more, publicly announced in period
millions of dollars

	1981	1982	1983	1984			Jan-May	
				Mar	Apr	May	1984	1983
Industrial countries	**56 022**	**42 571**	**38 742**	**33 022**	**4 330**	**2 861**	**52 613**	**15 358**
Australia	1 680	4 721	2 924	211	115	311	773	1 281
Belgium	360	1 172	883	—	—	—	—	83
Canada	4 112	3 838	967	—	137	380	1 152	200
Denmark	1 661	789	1 586	—	—	1 000	1 018	1 508
Finland	463	631	283	—	—	—	—	214
France	3 912	5 703	1 700	—	548	—	742	582
Greece	1 039	770	1 085	400	—	—	400	542
Ireland	1 361	401	764	—	—	—	—	541
Italy	6 030	3 757	2 980	283	19	56	980	1 324
Norway	713	1 769	1 236	24	—	—	24	286
Portugal	1 590	1 388	913	110	—	—	296	300
South Africa	287	1 479	752	—	50	100	250	575
Spain	3 242	1 849	3 041	235	245	192	1 072	1 753
Sweden	1 867	649	3 188	—	300	—	300	2 350
United Kingdom	747	1 635	1 328	107	450	278	1 595	348
United States	54 784	6 516	12 948	31 170	1 295	150	41 807	2 553
Yugoslavia	684	719	615	—	—	10	10	615
*Other**	1 490	4 785	1 549	482	1 171	384	2 194	303
Developing countries	**45 264**	**41 519**	**32 933**	**1 223**	**5 433**	**794**	**16 726**	**20 066**
Latin American countries	**30 152**	**26 719**	**15 406**	—	**3 845**	**86**	**10 631**	**11 711**
Argentina	2 534	1 565	1 750	—	—	—	—	—
Brazil	5 751	5 716	4 475	—	—	—	6 500	4 475
Chile	2 204	1 194	1 319	—	—	—	—	1 300
Colombia	1 030	741	549	—	—	—	170	100
Ecuador	934	815	431	—	—	—	—	—
Mexico	7 530	7 953	5 138	—	3 800	—	3 800	5 100
Peru	1 407	1 069	500	—	10	—	10	466
Venezuela	7 559	6 799	237	—	—	—	—	237
*Other***	1 203	867	1 007	—	35	86	151	33
Asian countries	**10 288**	**8 403**	**8 824**	**989**	**903**	**295**	**4 079**	**5 180**
India	377	284	809	155	20	—	225	477
Indonesia	725	1 250	1 467	17	—	30	812	1 146
Korea	2 824	2 923	3 250	717	383	201	1 704	1 262
Malaysia	1 725	1 909	950	—	500	—	650	860
Pakistan	350	455	365	—	—	—	—	340
Philippines	1 257	635	815	—	—	—	—	685
Thailand	692	268	349	—	—	—	247	18
Other	2 338	679	819	100	—	64	441	392
Middle Eastern and African countries	**4 824**	**6 397**	**8 703**	**234**	**685**	**413**	**2 016**	**3 175**
Algeria	—	26	1 934	—	—	20	20	700
Egypt	63	353	335	—	—	—	—	71
Morocco	774	326	226	—	20	—	115	25
Nigeria	1 802	2 042	1 775	—	—	—	—	33
Turkey	100	2 042	1 106	—	150	50	550	366
United Arab Emirates	363	93	876	—	39	—	39	690
Other	1 722	3 280	2 451	234	476	343	1 292	1 290
Centrally planned countries	**1 791**	**765**	**1 212**	**410**	**350**	**109**	**1 723**	**233**
East Germany	470	8	392	50	—	—	50	—
Hungary	550	340	683	—	350	—	762	233
Soviet Union	25	374	68	—	—	—	365	—
*Other***	746	43	69	360	—	109	546	—
International organizations****	**302**	**160**	**1 321**	—	—	—	—	**21**
Total	**133 379**	**85 015**	**74 208**	**34 655**	**10 113**	**3 764**	**71 062**	**35 678**

*Includes multinational organizations. **Includes unallocated. ***Includes COMECON institutions. ****Includes regional development organizations.

Eurocurrency market size

measured by foreign currency liabilities
at end of period, billions of dollars

	1977	1978	1979	1980	1981	1982	1983			
						Dec	Mar	Jun	Sep	Dec
Gross market size	740	949	1 233	1 524	1 861	2 057	2 074	2 045	2 115	2 153
Nonbanks	135	174	245	327	428	474	472	489	515	527
Official monetary institutions	100	115	145	150	132	90	90	84	90	89
Other banks	505	660	843	1 047	1 301	1 493	1 512	1 472	1 510	1 537
Eurodollars as % of gross	76	74	72	75	78	79	80	80	80	80

Central bank discount rates

at or near end of month

	1980	1981	1982	1983			1984	Current	
	Dec	Dec	Dec	Jun	Sep	Dec	Mar	Jun 1 1984	effective since
United States	13.00	12.00	8.50	8.50	8.50	8.50	8.50	9.00	Apr 9, 84
Canada	17.36	14.66	10.05	9.42	9.49	9.96	10.78	11.54	May 31, 84
Austria	6.75	6.75	4.75	3.75	3.75	3.75	4.25	4.25	Mar 14, 84
Belgium	12.00	15.00	11.50	9.00	9.00	10.00	11.00	11.00	Feb 16, 84
Denmark	11.00	11.00	10.00	7.50	7.50	7.00	7.00	7.00	Oct 27, 83
Finland	9.25	9.25	8.50	8.50	9.50	9.50	9.50	9.50	Jul 1, 83
France	9.50	9.50	9.50	9.50	9.50	9.50	9.50	9.50	Aug 31, 77
Germany	7.50	7.50	5.00	4.00	4.00	4.00	4.00	4.00	Mar 18, 73
Ireland	12.75	17.15	14.35	13.80	12.20	11.50	11.50	12.00	May, 84
Italy	16.50	19.00	18.00	17.00	17.00	17.00	16.00	16.00	Feb 15, 84
Netherlands	8.00	8.00	5.00	4.50	5.00	5.00	5.00	5.00	Sep 9, 83
Norway	9.00	9.00	9.00	8.00	8.00	8.00	8.00	8.00	Jun 6, 83
Portugal	18.00	18.00	19.00	23.00	25.00	25.00	25.00	25.00	Aug 10, 83
Spain	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	Jul 26, 77
Sweden	12.00	11.00	10.00	8.50	8.50	8.50	8.50	8.50	Apr 8, 83
Switzerland	3.00	6.00	4.50	4.00	4.00	4.00	4.00	4.00	Mar 18, 83
United Kingdom	14.00	14.37	10.00	9.56	9.50	9.00	8.50	9.00	May 10, 84
Japan	7.25	5.50	5.50	5.50	5.50	5.00	5.00	5.00	Oct 22, 83
New Zealand	14.00	13.00	13.00	13.00	13.00	13.00	13.00	13.00	Jul, 81
South Africa	7.00	13.50	13.50	13.50	13.50	13.50	13.50	13.50	Dec 12, 81
Argentina	87.01	98.50	128.54	161.87	183.75	183.75	134.13	167.37	Apr 1, 84
Korea	15.50	10.50	5.00	5.00	5.00	5.00	5.00	5.00	Mar 29, 82
Philippines	4.54	6.69	6.30	6.51	6.91	8.05	8.37	8.37	Mar, 84
Singapore	10.50	9.50	7.00	7.00	7.00	7.00	7.00	7.00	Feb 19, 82
Thailand	13.50	14.50	12.50	11.50	11.50	13.00	13.00	13.00	Dec 9, 83
Venezuela	13.00	14.00	13.00	11.00	11.00	11.00	11.00	11.00	May 18, 83

Day-to-day money rates

monthly averages

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States	18.90	12.37	8.95	9.45	9.48	9.34	9.47	9.56	9.59	9.91	10.29
Canada	15.61	14.53	10.63	9.25	9.35	9.43	8.78	9.60	9.63	9.50	9.72
Austria	11.50	7.50	6.00	5.00	5.62	5.62	5.75	5.87	5.87	6.00	6.38
Belgium	9.68	12.78	9.43	6.38	6.89	8.58	8.65	8.03	7.57	11.20	11.37
Finland	12.50	11.30	11.50	16.67	16.95	16.70	16.70	17.50	17.50	17.50	16.77
France	10.87	15.46	12.88	12.56	12.35	12.37	12.27	12.39	12.30	12.48	12.15
Germany	9.13	10.65	6.07	5.43	5.53	5.59	5.60	5.61	5.55	5.52	5.53
Ireland	13.31	16.88	14.54	12.62	11.00	12.25	12.19	12.12	11.25	10.75	12.12
Italy	17.50	20.63	19.00	17.69	17.75	17.79	17.88	17.91	17.67	17.25	17.25
Netherlands	8.37	10.67	5.31	5.68	5.82	5.70	5.84	5.77	6.12	6.13	5.79
Norway	11.00	18.60	11.00	12.30	13.50	13.00	13.00	12.80	11.45	13.00	13.00
Spain	16.74	18.73	20.30	19.85	20.27	18.56	16.41	10.16	18.14	14.75	11.54
Sweden	11.41	13.82	8.63	11.30	12.00	11.97	11.48	11.36	10.90	10.15	9.65
Switzerland	5.75	3.38	1.25	2.00	1.75	1.62	1.88	1.00	1.62	2.25	2.00
United Kingdom	13.00	9.13	6.70	7.30	7.81	7.06	7.77	7.31	7.12	7.08	6.25
Australia	9.51	12.84	11.04	9.80	9.03	9.31	4.56	7.09	9.05	11.21	13.45
Japan	9.49	6.70	6.92	6.53	6.43	5.99	6.47	6.05	6.04	6.05	5.88
South Africa	6.03	12.75	14.15	14.94	14.75	15.05	16.06	17.13	17.25	17.25	17.25
Argentina	70.84	84.93	155.32	175.30	178.30	178.30	178.30	138.61	128.53	128.52	161.88
Brazil	62.71	103.74	150.42	193.91	192.62	193.91	184.69	224.27	295.48	268.44	n.a.
Hong Kong	14.05	10.75	9.13	13.25	18.00	10.00	13.90	7.25	3.31	7.32	9.00
Korea	14.82	14.40	13.84	12.80	12.80	12.90	11.40	11.30	10.50	10.00	11.70
Philippines	15.70	14.70	16.12	16.54	24.23	18.96	31.18	25.52	21.76	9.99	n.a.
Singapore	10.23	3.96	11.45	6.51	7.02	7.23	7.05	6.92	6.83	7.64	8.13

Treasury bill rates

bond equivalent yields, at or near end of month

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States	14.87	11.90	8.15	9.05	8.92	9.05	9.28	9.20	9.48	10.09	10.02
Canada	17.01	14.41	9.80	9.24	9.24	9.38	9.71	9.73	9.79	10.53	10.59
Belgium	12.75	16.00	12.25	9.25	9.50	10.85	10.85	10.85	12.25	12.25	11.75
Ireland	12.84	17.35	14.70	12.12	11.96	11.66	11.63	11.80	12.16	12.59	12.35
Italy	16.87	21 36	19.11	17.18	17.08	17.05	16.95	15.74	15.81	15.61	15.45
Netherlands	8.00	9.75	5.62	5.87	5.62	5.62	5.63	5.75	6.12	5.88	5.38
Spain	n.a.	n.a.	15.28	14.60	14.52	14.53	14.46	13.61	13.66	13.20	12.64
Sweden	n.a.	n.a.	12.90	12.20	12.10	12.10	11.75	11.10	11.15	10.80	10.99
United Kingdom	13.45	15.31	9.90	9.21	8.89	9.08	9.08	9.08	9.08	8.59	8.59
Australia	12.17	13.27	9.39	10.34	9.38	9.32	8.54	9.43	10.35	13.11	11.89
Japan	5.93	5.42	5.42	5.42	4.91	4.91	4.91	4.91	4.91	4.91	4.91
New Zealand	11.25	11.25	11.25	7.80	7.80	7.80	7.80	7.80	7.80	7.80	7.80
South Africa	6.31	14.55	14.62	14.91	15.66	17.47	18.43	18.55	18.57	18.57	18.64
Brazil	65.87	92.62	115.40	163.92	179.15	179.15	179.15	179.15	179.15	179.15	n.a.
Mexico	27.73	33.33	57.44	56.17	54.50	53.85	53.78	53.02	n.a.	n.a.	n.a.
Philippines	12.70	13.22	14.54	14.83	15.13	15.63	15.99	16.27	17.01	17.25	n.a.
Singapore	6.77	3.03	2.74	2.55	2.63	2.62	2.59	2.67	2.65	2.66	2.87

Representative money market rates

bond-equivalent yields on major short-term (mostly 3-4 month) money market instruments other than Treasury bills, at or near end of month

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States	17.62	12.78	8.81	9.36	9.26	9.31	9.75	9.36	9.68	10.30	10.50
Canada	17.50	15.25	9.95	9.40	9.40	9.60	9.87	9.85	9.95	10.70	10.75
Belgium	13.10	16.00	12.35	9.25	9.50	10.75	11.00	11.00	12.50	12.35	11.90
France	11.56	15.25	12.75	12.50	12.19	12.31	12.19	12.25	12.54	12.56	12.31
Germany	10.20	10.50	6.20	5.80	6.15	6.25	6.30	6.10	5.85	5.80	5.70
Ireland	13.62	18.50	15.75	12.69	12.53	12.37	12.19	12.25	12.56	13.00	12.88
Italy	17.37	21.00	19.00	17.50	17.63	17.88	17.88	17.88	17.00	17.25	17.25
Netherlands	9.37	11.00	5.25	6.25	6.12	6.31	6.00	5.94	6.00	6.06	5.88
Portugal	11.00	13.80	15.04	22.30	23.00	24.17	24.11	24.06	23.79	23.99	24.04
Spain	17.40	15.52	16.55	22.06	22 19	20.29	18.48	17.30	18.30	16.42	15.07
Switzerland	7.50	10.12	3.87	4.25	4.25	4.25	3.87	3.62	3.75	3.94	3.88
United Kingdom	14.75	15.69	10.50	9.56	9.31	9.25	9.31	9.37	9.21	8.88	8.81
Australia	13.00	16.00	10.65	11.15	11.00	10.60	9.50	11.00	13.00	13.55	14.20
Japan	9 80	0 30	6.80	6.62	6.30	6.42	6.42	6.30	6 40	6.40	6.20
New Zealand	14.25	16.05	16.75	10.00	10.75	12.00	12.10	13.85	15.00	14.75	15.00
South Africa	7.12	15.47	15.26	16.45	16.94	18.19	19.12	19.07	19.01	18.30	19.07
Chile	26.79	34.54	71.44	25.34	25.34	25.34	22.42	19.56	14.03	11.35	18.16
Hong Kong	17.69	14.18	10.13	12.75	16.88	11.50	12.84	11.37	7.87	7.90	9.93
Indonesia	12 54	14.48	18.50	16.50	15.00	15.00	19.50	19.00	20.50	19.50	n.a.
Korea	16.35	15.69	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00
Malaysia	9.41	9.50	8.50	8.10	8.20	8.65	9.80	9.47	8.51	8.95	9.10
Philippines	14.99	17.70	15.96	16.49	15.98	17.34	15.61	16.08	17.41	17.14	n.a.
Singapore	14.12	7.81	8.69	7.37	7.50	7.62	8.44	7.75	7.75	8.50	8.63
Taiwan	14.49	10.94	9.94	8.37	7.82	7.26	7.65	9.22	9.42	7.81	7.31
Thailand	16.55	14.29	12.25	14.00	14.25	14.50	16.00	16.50	17.00	15.50	13.50

Commercial bank deposit rates

at or near end of month

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States	16.25	12.62	8.25	9.20	9.30	9.30	9.70	9.40	9.77	10.35	10.50
Canada	17.00	15.20	9.85	9.35	9.35	9.50	9.82	9.80	9.90	10.65	10.70
Austria	11.25	9.63	6.25	6.06	6.31	6.37	6.50	6.50	6.25	6.44	6.56
Belgium	12.63	15.50	12.25	9.50	9.38	11.25	11.25	10.87	12.37	11.75	11.50
Denmark	10.00	10.00	9.00	6.50	6.00	6.00	6.00	6.00	6.00	6.00	6.00
Finland	5.00	5.00	4.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25	5.25
France	11.25	9.16	8.24	7.80	7.70	7.70	7.66	7.72	7.76	7.76	7.76
Germany	8.00	9.50	6.00	5.63	5.60	5.80	5.90	5.65	5.40	5.35	5.35
Ireland	13.62	18.38	15.25	12.25	12.50	12.25	11.75	11.87	12.37	12.63	12.50
Italy	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25	13.25
Netherlands	9.50	11.00	5.37	6.12	6.06	6.19	6.13	5.94	6.00	6.06	5.75
Norway	11.00	12.75	13.50	12.50	12.50	12.50	12.75	13.00	12.50	12.75	12.75
Portugal	12.00	14.00	15.00	21.50	21.50	21.50	21.50	21.50	21.50	21.50	21.50
Spain	4.50	11.78	12.53	12.24	12.08	12.50	12.62	12.49	12.52	12.35	n.a.
Sweden	13.20	12.65	12.15	12.05	12.20	12.30	11.70	11.00	11.10	10.65	10.65
Switzerland	7.50	8.75	3.00	3.75	3.50	3.50	3.50	3.25	3.25	3.00	3.00
United Kingdom	14.87	15.69	10.31	9.50	9.25	9.22	9.31	9.37	9.25	8.88	8.91
Australia	12.71	15.65	10.20	10.56	10.96	10.35	10.40	11.25	12.20	13.13	13.36
Japan	9.00	6.50	7.00	6.88	6.45	6.60	6.50	6.52	6.63	6.50	6.35
New Zealand	13.50	15.50	16.50	9.00	9.50	10.75	11.50	13.75	10.00	10.00	14.75
South Africa	7.87	14.75	15.25	17.00	17.00	18.43	20.13	19.45	18.88	19.38	18.88
Argentina	72.00	86.76	103.42	176.41	176.41	176.41	176.41	139.91	121.66	121.66	158.17
Brazil	54.00	110.05	21.00	25.00	26.00	24.00	23.00	26.00	25.00	23.00	n.a.
Chile	39.45	36.87	57.72	25.19	25.19	25.19	22.28	19.74	12.95	11.09	18.16
Hong Kong	13.00	12.50	7.50	12.00	10.00	9.00	9.00	7.00	5.50	5.50	8.00
Korea	14.82	14.40	7.60	7.60	7.60	7.60	7.60	6.00	6.00	6.00	6.00
Malaysia	8.60	10.00	8.40	7.15	7.15	7.60	7.75	7.75	7.75	7.83	7.83
Mexico	26.15	31.82	52.54	56.38	55.20	54.84	54.70	53.86	n.a.	n.a.	n.a.
Philippines	14.00	13.35	14.10	13.47	13.62	14.93	14.96	14.33	15.57	15.37	n.a.
Singapore	13.19	7.50	8.25	6.81	7.07	7.19	7.44	7.13	7.19	7.69	8.01
Taiwan	10.25	10.75	7.50	7.00	7.00	7.00	7.00	7.00	7.00	7.00	7.00
Thailand	9.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00
Venezuela	16.00	14.75	15.50	12.50	12.00	12.00	12.00	11.50	11.50	11.00	11.50

Domestic government bond yields

long-term issues, at or near end of month

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States	11.46	14.33	10.61	11.65	11.85	11.89	12.00	11.72	12.13	12.49	12.79
Canada	12.69	15.27	11.69	11.76	11.73	11.80	12.02	11.92	12.40	13.06	13.31
Austria	9.62	10.37	8.81	8.32	8.16	8.06	8.02	7.96	7.88	7.88	7.94
Belgium	13.04	13.99	12.66	11.39	11.32	11.75	11.89	11.97	12.35	12.20	12.08
Denmark	19.98	20.91	20.14	14.19	13.95	14.22	12.96	13.39	14.02	14.78	14.27
Finland	10.42	10.98	10.64	10.97	11.19	11.16	11.16	11.17	10.62	11.19	10.80
France	14.31	16.44	15.40	14.03	14.15	14.12	13.96	13.76	13.78	14.05	13.81
Germany	9.19	9.71	7.90	8.43	8.30	8.34	8.38	8.33	8.13	8.18	8.18
Ireland	15.63	18.28	14.54	13.72	13.82	13.72	14.25	13.94	14.16	14.08	14.14
Italy	16.23	21.39	19.70	17.82	17.65	17.78	17.69	16.91	16.34	15.69	15.74
Netherlands	10.48	11.28	8.16	8.80	8.53	8.57	8.58	8.57	8.56	8.40	8.45
Norway	10.44	12.37	13.32	12.50	12.50	12.50	12.50	12.50	12.25	12.25	12.25
Portugal	17.19	17.39	16.63	21.97	22.05	22.80	22.11	21.19	21.57	n.a.	n.a.
Spain	16.15	16.20	15.92	18.76	19.47	19.50	18.71	18.33	18.68	18.74	n.a.
Sweden	12.61	12.80	13.01	12.20	12.24	13.05	12.30	11.70	11.50	11.50	11.65
Switzerland	4.63	5.40	4.22	4.71	4.61	4.62	4.52	4.31	4.38	4.55	4.47
United Kingdom	13.05	15.02	10.62	10.15	10.13	9.93	9.94	9.97	10.04	9.89	10.16
Australia	13.00	15.00	13.00	14.40	13.70	13.40	13.65	13.70	14.05	14.00	14.00
Japan	9.04	8.32	7.76	7.58	7.51	7.39	7.19	7.20	7.06	6.74	6.68
New Zealand	12.99	12.55	12.84	10.13	10.58	10.61	10.50	10.84	11.33	n.a.	n.a.
South Africa	11.81	13.33	11.31	13.14	13.29	13.60	13.70	14.18	13.52	14.20	14.63
Philippines	13.20	13.01	13.64	13.95	13.28	13.76	14.47	14.42	14.61	13.67	n.a.
Venezuela	7.39	12.50	15.00	14.00	14.00	14.00	13.50	13.00	13.00	13.00	13.50

Commercial bank lending rates to prime borrowers

at or near end of month

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep[1]	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States	21.50	15.75	11.50	11.00	11.00	11.00	11.00	11.00	11.00	11.50	12.00
Canada	18.25	16.50	12.50	11.00	11.00	11.00	11.00	11.00	11.00	11.50	11.50
Austria	12.50	13.50	11.75	9.25	9.25	9.25	9.25	9.25	9.25	9.25	9.25
Belgium	15.75	18.00	15.50	12.50	12.50	13.25	13.75	13.75	14.75	14.75	14.75
Denmark	13.75	15.00	14.00	10.50	10.50	10.00	10.00	10.00	10.00	10.00	10.00
Finland	9.83	9.84	8.95	10.16	10.14	10.15	10.18	10.30	10.36	10.38	n.a.
France	12.25	14.00	12.25	12.25	12.25	12.25	12.25	12.25	12.25	12.25	12.25
Germany	11.50	13.00	8.75	7.75	7.75	7.75	7.75	7.75	7.75	7.75	7.75
Ireland	14.50	17.25	16.50	13.75	13.75	13.75	13.75	13.75	13.75	13.75	13.75
Italy	20.50	22.50	20.75	18.75	18.75	18.75	18.75	18.50	18.50	17.50	17.50
Netherlands	10.75	12.00	6.25	7.00	6.75	6.50	7.00	6.75	6.75	6.75	6.50
Norway	12.50	13.75	14.50	13.50	13.25	13.75	13.50	13.63	13.75	13.30	13.30
Portugal	18.75	20.50	23.50	30.00	30.00	30.00	30.00	30.00	30.00	30.00	30.00
Spain	18.50	17.04	19.00	24.09	23.70	22.87	20.85	20.01	20.55	19.44	n.a.
Sweden	14.00	15.00	15.00	13.50	13.50	13.50	13.50	13.50	13.50	13.50	13.50
Switzerland	5.75	8.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00	6.00
United Kingdom	14.00	14.50	10.00	9.50	9.00	9.00	9.00	9.00	9.00	8.50	8.50
Australia	13.50	15.75	15.00	14.00	13.25	13.25	12.75	11.50	13.00	14.00	15.50
Japan	8.16	6.95	6.28	6.23	6.23	6.08	5.89	5.81	5.77	5.80	5.80
New Zealand	13.00	13.00	13.00	11.00	11.00	11.00	11.00	11.00	11.00	11.00	11.00
South Africa	9.50	17.00	18.00	18.00	18.00	19.00	20.00	20.00	20.00	20.75	20.75
Argentina	77.00	92.60	109.50	188.58	188.58	188.58	188.58	152.08	133.83	133.83	170.33
Brazil	120.10	152.40	23.81	24.00	24.00	24.00	24.00	24.00	24.00	24.00	n.a.
Chile	49.55	61.43	85.19	39.83	40.60	40.40	35.11	31.43	22.75	21.26	34.35
Hong Kong	17.00	16.00	10.50	16.00	15.00	13.50	13.50	11.50	10.00	10.00	12.00
Indonesia	21.00	19.25	22.00	19.50	19.50	19.50	19.75	20.00	21.25	21.50	21.50
Korea	19.50	16.50	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00	10.00
Malaysia	8.50	12.00	12.50	11.00	11.00	11.00	11.00	11.00	11.00	11.00	11.00
Mexico	24.25	31.81	46.12	57.78	57.14	56.82	56.44	55.95	55.16	53.11	51.10
Philippines	16.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00	18.00	22.00	n.a.
Singapore	13.60	11.83	9.33	8.95	8.93	8.93	8.98	9.05	9.03	9.20	9.63
Taiwan	16.20	15.25	10.75	10.25	10.25	10.25	10.25	10.25	10.25	10.25	10.25
Thailand	16.50	17.00	16.00	15.50	15.50	15.50	16.00	16.00	16.50	17.00	17.00
Venezuela	15.00	15.50	17.00	16.00	16.00	16.00	16.00	16.00	14.50	14.50	15.00

Domestic corporate bond yields

long-term issues, at or near end of month

	1980	1981	1982	1983				1984			
	Dec	Dec	Dec	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
United States	13.00	15.50	11.75	12.25	12.63	12.38	12.63	12.38	12.88	13.25	13.88
Canada	13.53	16.18	12.74	12.54	12.57	12.58	12.89	12.78	13.27	13.84	14.13
France	15.23	17.33	15.91	14.36	14.62	14.30	14.06	13.96	14.28	14.37	14.23
Germany	9.50	10.50	8.20	8.30	8.30	8.30	8.30	8.30	8.00	8.00	8.00
Netherlands	10.71	11.03	7.80	8.68	8.39	8.53	8.51	8.44	8.39	8.26	8.28
Norway	11.24	13.36	14.13	13.25	13.25	13.25	13.25	13.25	13.00	13.00	13.00
Spain	14.82	14.76	17.10	20.05	20.37	20.03	19.84	20.19	20.69	21.90	22.54
Sweden	11.95	12.94	13.37	12.99	12.40	12.51	12.21	12.15	11.96	11.84	12.04
Switzerland	n.a.	n.a.	4.87	5.07	4.94	4.94	4.94	4.93	4.91	4.85	4.91
United Kingdom	14.21	16.65	12.34	11.89	11.84	11.51	11.57	11.52	11.61	11.29	11.48
Australia	14.25	16.50	15.00	15.00	15.00	15.00	13.50	14.00	14.50	14.50	n.a.
Japan	8.60	7.70	7.55	7.30	7.29	7.27	7.09	7.05	7.04	6.92	6.89
Korea	28.20	26.90	15.90	14.20	14.10	14.20	14.20	14.30	14.00	13.60	13.00
Venezuela	16.15	17.00	18.00	18.00	18.00	18.00	18.00	18.00	17.50	17.50	17.50

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B6200-2A

World Financial Markets

Morgan Guaranty Trust Company of New York

July 1984

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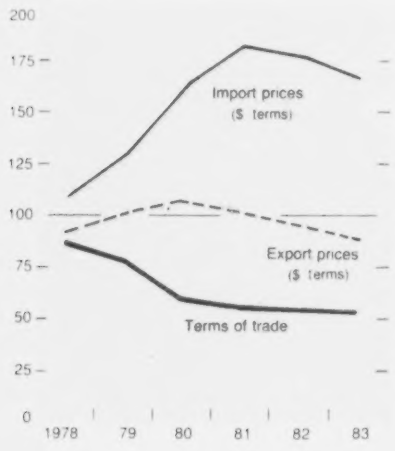
Chart 1

Terms of trade

Indices, 1977 = 100



Stabilization policies in Brazil

Brazil has been making a determined effort, especially since early 1983, to improve its balance of payments and lower domestic inflation. The government has made major changes in foreign-sector, wage, fiscal, and monetary policies to pursue these twin purposes. Excellent results already have been achieved in the external area: last year, Brazil registered an unprecedented merchandise trade surplus of $6½ billion, and in the first six months of 1984 an additional surplus of $6 billion has been posted. The trade account improvement, together with additional credit from commercial banks and other sources of external finance, has enabled the central bank to clear up all the arrears accumulated in 1983 as well as to begin to rebuild its foreign exchange reserves. Moreover, because the improving trade performance increasingly derives from rapid export growth at an annual rate of over 20% rather than compression of imports, Brazil is achieving a decline in its high debt to exports ratio — a key indicator of creditworthiness. It is further benefiting from a recovery of output and incomes in export-oriented agriculture, mining, and industry. Real GDP, which fell by a cumulative 4% in 1981-83 and almost 11% in per capita terms, may well record a small gain this year.

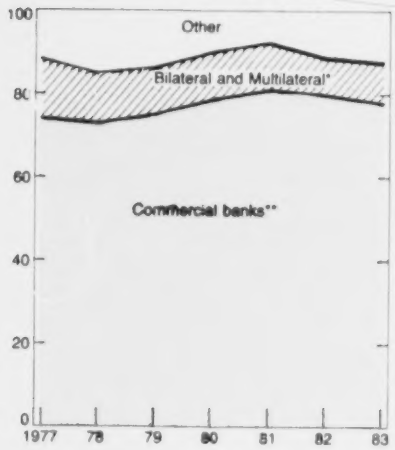
In the domestic area, in contrast, the results so far are mixed if not disappointing. Wage policy has undergone a significant change for the better, and now that real wages have declined, the rise in labor costs is no longer a contributing factor to inflation. The cash or operational deficit of the public sector has been all but eliminated by holding down current and investment outlays. Interest rates are being set more realistically and credit subsidies have been limited. Nonetheless, the overall fiscal deficit remains quite large (about 17% of GDP) because of the growing cost of servicing the indexed domestic debt of the public sector. The monetary aggregates have accelerated. The rate of inflation has not come down: the widely used "general" price index has risen an average of close to 10% per month since the beginning of the year for a cumulative total of 76%, versus 67% in January-June of 1983 and 47% in the first half of 1982.

To sustain the modest economic recovery now in place, permit a deceleration of inflation, and maintain the balance of payments gains, Brazil should further reduce the fiscal imbalance. In view of the heavy bur-

Chart 2

Total external debt by creditor

end-December, as percent of total



* Excluding the IMF

**Including Brazilian banks abroad

den imposed by the outstanding stock of indexed obligations, there is no escaping from the need to generate a strong surplus in the operational accounts of the public sector. To this end, clear investment priorities must be established and reliance on loans to finance projects must be reduced; remaining costly subsidies to consumption and production must be phased out; and the financial problems of the ailing social security and savings and loan systems must be tackled. A fiscal deficit reduction of at least 2%-3% of GDP per annum would enable the monetary authorities gradually to regain control over the money supply, setting the basis for a lower rate of inflation. Moreover, by lessening the overwhelming absorption of available domestic and foreign savings by the public sector, such a deficit reduction would make room for growth of private-sector investment. It also would minimize dependence on external borrowing and permit the restoration of normal credit market access and creditworthiness so important to assure a high rate of economic growth in the long run.

Background

Throughout the 1970s and until 1981, Brazil followed a development strategy that maximized public and private investment, but with little regard for its economic and financial costs. Massive infrastructure, import-substitution, and natural resource projects were carried out by a swelling number of large private and government-owned corporations. The investments were underwritten by a complex web of subsidized bank credit lines, tax concessions, import tariffs, and guarantees on domestic and foreign borrowing. The enormous costs were borne through higher taxes, compulsory savings, and heavy domestic and external borrowing. Gradually, direct and indirect involvement in the development process compromised the government's ability to manage aggregate demand in a noninflationary manner, particularly in the aftermath of adverse external shocks.

Brazil suffered from three such exogenous shocks during the 1979-82 period. The first was a steep, 45%, decline in the terms of foreign trade relative to 1977 (see Chart 1). This was attributable mainly to the escalation in petroleum import prices that started in 1979. In response, the country embarked on a large-scale petroleum exploration, substitution, and conservation program. Petrobras, a state-owned enterprise with a virtual monopoly on oil production, imports, and refining, stepped up its drilling activity and found substantial quantities of hydrocarbons. The increased reserves allowed a major expansion of petroleum production, from 170 thousand barrels per day (bpd) in 1979 to 270 thousand bpd in 1982 and a current rate of 500 thousand bpd.

The substitution effort relied on the exploitation of alternative energy sources, particularly alcohol, coal, natural gas, and hydroelectric power. The alcohol program, for example, subsidized the planting of sugarcane and its conversion to a fuel suitable for automobiles. It yielded the equivalent of about 130 thousand bpd of petroleum last year, versus about 10 thousand bpd when started in 1976. Meanwhile, oil consumption, discouraged through higher prices, fell from over 1.1 million bpd in 1979 to 960 thousand bpd in 1983 (see Table 1). Brazilian petroleum consumption last year was 18% lower per unit of output than in 1979, while oil self-sufficiency has risen from 15% to 50% as of mid-1984. The energy program has thus made possible a dramatic cut in net oil imports, from 1 million bpd in 1979 to

Table 1

Petroleum demand and supply

thousands of barrels per day

	Consumption	Production	Net imports
1978	945	166	871
1979	1,134	171	994
1980	1,125	187	877
1981	1,030	220	773
1982	1,020	268	732
1983	961	339	638

640 thousand bpd last year and an estimated 480 thousand bpd in 1984.

Despite reduced import demand, the cumulative cost to Brazil of the increase in world oil prices over the four years from 1979 to 1982 was $19 billion, or the equivalent of a year's exports, as measured by the difference between actual and pre-1979 petroleum prices times the net volume imported.

The second shock was the sharp rise in international interest rates. LIBOR moved up from 6½% in 1977 to a peak of about 19% in early 1980 and again in mid-1981, a rise that was all the more burdensome as the terms of trade deteriorated. Three complementary courses of action could have been pursued. New borrowings could have been minimized through restrictive demand management policies. Brazil did attempt on two occasions to implement economic adjustment programs without the supervision and financial support of the IMF. One try, in late 1979-early 1980, soon ended in failure. Another in 1981 was a modest success, mainly in cutting the value of nonpetroleum imports by 15%. However, neither program much reduced Brazil's foreign borrowing.

Sources of finance charging fixed or noncommercial interest rates could have been tapped more intensively. Although Brazil's indebtedness to official bilateral and multilateral agencies rose from $5.3 billion at the end of 1977 to $7½ billion by the end of 1981, it declined from 14% to 10% of total foreign debt. The funds obtained from these sources were much less in absolute and relative terms than, for example, the amounts secured by Korea during the same period. And whereas Korea also obtained IMF financial support, Brazil chose otherwise. Accordingly, its reliance on commercial bank debt at floating interest rates actually increased (see Chart 2).

A greater portion of new loans could have been contracted in currencies other than the dollar and at lower interest rates. However, data on the currency composition of Brazil's medium- and long-term foreign debt reveal no successful diversification away from the over-80% concentration in dollar-denominated loans between end 1977 and end 1981. A slight increase in the yen portion, from 4% to 6% of total loans, came at the expense of other nondollar indebtedness. All in all, the cumulative cost of the high international interest rates over the 1978-82 period was $10 billion, computed as the difference between actual and pre-1978 effective interest rates times the average annual external debt.

The third shock was the sudden drop in export volume in 1982. This stemmed mainly from the global recession, especially the import reductions in Brazil's Latin American and Eastern European markets and in the OPEC countries (see Table 2). The 1982 drop of 9% contrasts sharply with the 16% annual average export volume growth posted by Brazil during 1977-81 — especially the 22% annual average rate recorded in 1980-81. The $3.4 billion decline in non-oil exports was countered with a $1.9 billion cut in non-oil imports, thanks mainly to a tightening of import controls, and a $1.1 billion reduction in net petroleum imports (see Table 3).

These three adverse exogenous events severely disrupted the Brazilian economy — far more than had the 1973 oil shock. In the early 1970s, the country's GDP expanded in real terms by an annual average of 11½% and inflation (measured by the GDP deflator) ran at less than 20% per year. Following the first oil shock, the rate of economic growth fell to an annual average of 7% during 1974-78 and inflation ratcheted up to a remarkably constant average of about 40% per year.

Table 2

Destination of exports

billions of dollars

	1981	*1982*	*1983*
Total	23.29	20.18	21.90
*Latin America**	3.73	2.32	1.69
Eastern Europe	1.70	1.19	1.44
OPEC	2.44	1.89	2.00
United States	4.11	4.03	5.06
Europe	6.47	5.94	6.26
Japan	1.22	1.29	1.43
Canada	0.29	0.23	0.31
Other	3.33	3.29	3.71

*Venezuela and Ecuador included in OPEC.

Table 3

Foreign trade

billions of dollars

	Non-oil exports	Non-oil imports	Net oil imports	Trade balance
1977	12.5	—8.3	—3.6	0.6
1978	12.4	—9.5	—3.9	—1.0
1979	14.9	—11.6	—6.1	—2.8
1980	19.6	—13.0	—9.4	—2.8
1981	22.0	—11.1	—9.7	1.2
1982	18.6	—9.2	—8.6	0.8
1983	20.5	—7.2	—6.8	6.5

Table 4

Macroeconomic policy indicators

percent change from previous year-end, except where noted

	1980	1981	1982
Fiscal policy			
*Public-sector borrowing requirements**	83	261	150
% of GDP	8	13	17
Monetary policy			
M1	70	75	70
M3	72	115	104
Wage policy			
Minimum wages	97	106	98
Industrial wages (Sao Paulo)	110	96	108
*General prices***	110	95	100

*Percent change from previous year's total.

**Composite of consumer prices (with weight of 0.3) and construction costs (0.1) in Rio de Janeiro, and wholesale prices (0.6).

Then, in the wake of the last set of shocks, economic growth came to an abrupt halt and inflation accelerated to a new plateau of 100% during 1980-82.

The faltering growth performance and the protracted upsurge of inflation reflected the gradualist approach to adjustment that Brazil followed until 1983. There should have been prompt and forceful changes in relative prices (of energy, borrowed capital, and tradable goods) and also containment of aggregate demand through restrictive fiscal, monetary, and wage policies. Instead, changes in relative prices were delayed and insufficient, and attempts at stabilization were halfhearted. Brazil's approach stood in marked contrast with the far more successful but radical course followed by many developing countries in Asia facing similar circumstances.

Thus, while higher world oil prices eventually were passed on to Brazilian consumers, enormous sums were spent to develop and provide low-cost energy substitutes for imported petroleum. Some sectors of the economy were exposed to rising international interest rates, but credit subsidies were increased vastly for private-sector borrowers in such priority areas as agriculture, and the cost of credit was not allowed to interfere with the grandiose investment plans of the public sector. While export competitiveness was sustained and at times enhanced through currency depreciations and subsidies of all kinds, the high import barriers that had been erected for the sake of industrialization thwarted the growth of low-cost export industries.

At the same time demand management policies generally were unsupportive of noninflationary adjustment. Current and investment expenditures by the central, state, and municipal governments, as well as by myriad public enterprises, consistently outran tax and other revenues. On a consolidated basis, the annual borrowing requirements of the public sector rose from the equivalent of about 8% of GDP in 1979-80 to 13% of GDP in 1981 and 16½% of GDP in 1982 (see Table 4).

Formal targets for the monetary base and M1, established at the beginning of each year, were exceeded routinely due to lack of control over open-ended credit and consumer subsidies, large-scale foreign borrowing by the public and private sectors, and other expansionary measures. The domestic liabilities of the monetary authorities — defined broadly to incorporate the monetary base, treasury debt held by the public, and foreign-currency deposits at the central bank — jumped 60% in 1980, 150% in 1981, and over 90% in 1982. Broad money supply (M3) increased 72% in 1980, 115% in 1981, and 104% in 1982.

Beginning in 1979, policy mandated increases in wages that at a minimum were to be in line with actual inflation; it also granted lower-paid workers (those earning up to three times the minimum wage, constituting two-thirds of workers covered by legislation) an automatic, 10% annual raise above inflation; and it encouraged firms to award productivity raises of 3%-5% per year above the obligatory adjustments. Wages actually paid by industry in Greater Sao Paulo showed a cumulative 26% real increase during 1979-82.

The adjustment effort

The need for resolute economic adjustment became evident to the Brazilian authorities around the middle of 1982, when it proved increasingly difficult to finance the deficit in the current account of the balance of payments. The deficit, which had averaged nearly $12 billion per year during 1979-81, increased to an an-

Table 5

Current account

billions of dollars

	1982	1983 As projected in Jan 1983	1983 Actual	1984 As projected in Jan 1983	1984 As projected in Jan 1984	1984 Q1 Actual*
Non-oil exports	18.6	20.2	20.5	23.7	22.7	20.9
Non-oil imports	—9.2	—7.2	—7.2	—9.8	—8.8	—6.0
Net oil imports	—8.6	—7.0	—6.8	—5.9	—4.8	—5.0
Trade balance	0.8	6.0	6.5	8.0	9.1	9.9
Net interest payments	—11.4	—9.5	—9.6	—9.0	—10.6	—8.5
Net other services	—4.2	—3.5	—3.1	—4.0	—3.8	—2.6
*Current account***	—14.8	—7.0	—6.2	—5.0	—5.3	—1.2

*Annualized, not seasonally adjusted.

**Excluding a reinvested earnings debit of $1.6 billion in 1982 and $0.7 billion in 1983.

nualized rate of $15½ billion in the first half of 1982. In the first six months of that year, borrowings from commercial banks in the BIS-reporting area increased by $2.8 billion, sufficient to cover only 35% of the current account deficit. Moreover, a disproportionate share (three-quarters) of this amount was provided by U.S. banks, though they held only one-third of BIS-area bank claims on Brazilian residents. Access to international capital markets diminished further during the third quarter of 1982, in the aftermath of debt-servicing difficulties in Argentina and Mexico, even as the current account deficit was peaking at an annualized rate of $18 billion. The ensuing loss of foreign currency reserves seriously eroded Brazil's liquidity position. Emergency "bridge" loans from commercial banks, the U.S. Treasury, and the BIS had to be obtained in the final months of the year to keep payments from falling into arrears. Nevertheless, save for tighter import controls, major policy initiatives were deferred so as to avoid upsetting congressional, gubernatorial, and municipal elections held in November of 1982.

In January 1983 the government reached agreement with the IMF on a three-year economic program to be supported by an SDR 4.2 billion Extended Facility. The program's balance of payments objectives seemed ambitious — unprecedentedly large trade surpluses ($6 billion in 1983 and $8 billion in 1984, following a surplus of only $800 million in 1982), and correspondingly reduced current account deficits (see Table 5). The current account improvement targeted for 1983 was the equivalent of 2.3% of GDP, with an additional 0.7% of GDP to be achieved in 1984. This was to be made possible through minidevaluations running at least 1% per month ahead of domestic inflation, to enhance export competitiveness; further progress in energy self-sufficiency and conservation, leading to lower net petroleum imports; and overall demand containment projected to cause a 3½% fall in real GDP in 1983, with a consequent drop in non-oil imports.

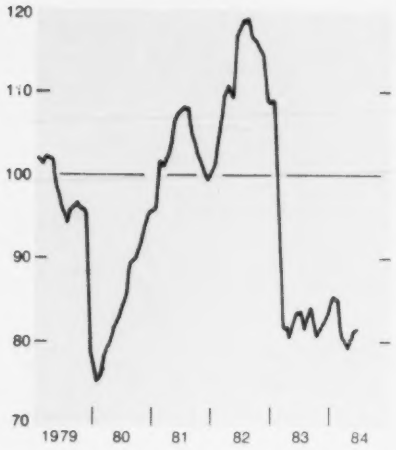
Domestic stabilization objectives included reducing the public-sector deficit by the equivalent of 6% of GDP in 1983 and a further 3% of GDP in 1984, from a then-estimated deficit of 14% of GDP in 1982; cutting back to 60% the growth of both the monetary base and M1, from 87% and 70%, respectively, in 1982; and attaining wage settlements "designed to increase employment," which in fact meant a new wage policy that would no longer grant raises in excess of inflation. These policies were intended to lower inflation from 100% in 1982 to 70% in 1983 and 40% in 1984.

Within a few weeks, however, it became apparent that the anticipated trade account improvement would not materialize without a swift change in incentives to export. Exports in January-February 1983 were running about 5% below, rather than well above, the first two months of 1982. Speculation against the cruzeiro was evident in that export deliveries slowed and the surrender of export receipts was delayed. Con-

Chart 3

Real effective exchange rate

index, 1980-82 = 100



sequently, the authorities decided in late February to devalue the currency by 30% against the dollar and to maintain the beneficial effect of this adjustment through further depreciation. Since late 1983, the cruzeiro has, in fact, been devalued strictly in line with domestic inflation. This single measure, which enhanced Brazilian competitiveness by 23% on a real effective basis during 1983 (see Chart 3), became the key to the fulfillment of the trade surplus objective. Alone among major Latin American countries, Brazil's non-oil exports increased 10% during 1983, or slightly more than expected, based on export gains in soybeans, steel, footwear, and chemicals. Sales to the United States rose 25%, offsetting market losses in Latin America. With real GDP declining 3.2%, very close to the projected 3½%, non-oil imports fell 21%, precisely as much as planned. Net petroleum imports dropped somewhat more than originally anticipated. The current account deficit improved by $8.6 billion, or about 4% of GDP, versus the intended improvement of less than 2½% of GDP.

The 1984 stage of the economic adjustment program calls for an even better external performance, with the initial trade surplus objective of $8 billion revised up to $9.1 billion at the beginning of this year. As of mid-1984, the issue no longer is whether the intended surplus will be attained, but by how much it will be exceeded — anywhere from $1 billion to $2 billion, depending mainly on the speed with which non-oil imports recover during the second half of the year. In the first five months, non-oil exports were up 23%, versus a projected 11% increase for the year as a whole. Non-oil imports were down 12½% instead of rising 22%. The United States continues to make a crucial contribution to Brazilian trade performance. Its imports from Brazil rose 54% in January-May 1984 from a year earlier. Brazil's trade surplus with the United States accounts for nearly half of its overall trade surplus. This is despite some protectionist moves against Brazilian steel. The deficit on current account should be on target at $5 billion or less even with the recent escalation in international interest rates.

The improved export performance, aside from generating welcome foreign exchange, is bringing benefits to Brazilian agriculture and industry. After several years of lackluster agricultural growth, farmers are planting almost 11% more land than in 1983 and the 1984 grain harvest is expected to be 14% higher than last year's. National industrial production, which fell a total of 15% during 1981-83, rose 4% in the first four months of 1984 relative to January-April of 1983. This was mainly because of increased shipments abroad by the steel, chemical, and paper industries, as well as higher domestic sales of tractors, fertilizers, and other inputs needed by farmers. In the industrial hub of Sao Paulo, where production for export accounted for 28% of total output in the first quarter of this year versus a mere 13% in 1979, the massive loss of jobs that took place in 1981-83 has ended and there are signs that employment is beginning to rise.

The adjustment of Brazil's internal performance, in contrast to its external accounts, has proceeded very slowly. Among the major tools of economic policy, only wage policy has ceased to feed inflation. The applicable legislation was altered in various stages during 1983 to permit the partial deindexation of wages. The final compromise bill, approved in October, mandated that workers earning less than three times the minimum wage receive raises no higher than the increased cost of living, and that better-paid workers be awarded raises well below the

Table 6

Public-sector borrowing requirements

percent of GDP

	1981	*1982*	*1983*
Total	13.1	16.5	19.5
*Operational**	6.2	6.9	2.7
Monetary correction	6.9	9.6	16.8
Central administration	3.9	5.6	4.7
*Operational**	1.6	2.1	—0.1
Monetary correction	2.3	3.5	4.8
State enterprises	5.8	7.1	9.7
*Operational**	3.1	3.6	2.5
Monetary correction	2.7	3.5	7.2
State and municipalities	3.4	4.2	5.7
*Operational**	1.3	1.3	0.8
Monetary correction	2.1	2.9	4.9
Other institutions	0.0	—0.4	—0.6
*Operational**	0.2	—0.1	—0.5
Monetary correction	—0.2	—0.3	—0.1

*Difference between current revenues and current and investment expenditures (including interest payments above monetary correction).

rate of inflation. The change in wage policy has been instrumental in reducing current government spending: the public-sector wage bill fell by about 15% in real terms last year and perhaps an extra 10% in the first half of 1984. This has minimized the need for layoffs. Also, it has helped the cost competitiveness of companies in the private sector, enabling them to keep workers rather than fire them as they had done in 1981-82. Wages paid by industry in Greater Sao Paulo lagged the local cost of living by 8% in 1983 and may have fallen behind by an additional 15% since December.

In the fiscal area, the expected reduction in the overall deficit has not materialized (see Table 6). The operational portion of the deficit has been cut from the equivalent of 7% of GDP in 1982 to almost zero in the first half of 1984. However, this has been more than offset by a jump in the deficit due to the indexation of public-sector debt. The indexation cost rose by over 7% of GDP last year and is not expected to fall during 1984.

The major contributors to lower government expenditures in real terms are the fall in the public-sector wage bill and significant reductions in investment outlays. State-owned enterprises were required to cut back investments by about 30% in real terms in 1983. Another large contraction, of perhaps 20%, is in store for 1984. Capital expenditures at all levels of government in such areas as transportation and nuclear energy have been restrained the most severely, while programs in petroleum exploration and electric power have been spared.

The raising of revenues through taxation and price increases on government-supplied goods and services has been much more difficult than anticipated. The effects of recession and wage declines on taxable corporate and personal incomes, and of high inflation on evasion and collection lags, have thwarted all attempts to increase treasury tax revenues in real terms. Thus, despite improvements in tax administration and the imposition of additional income and other taxes (particularly on capital gains and financial transactions), treasury revenues fell 4% in real terms during 1983 and 7% in the first five months of 1984 relative to the same period last year. Meanwhile, administered price increases on fuel, steel, electricity, and other goods or services provided by the public sector were subject to periodic delay in 1983, although adjustment lags have been shortened so far this year.

Reduction of subsidies and other transfer payments have fallen far short of their potential contribution to the fiscal adjustment effort, especially last year. Until mid-1983, after more than three years of triple-digit inflation, subsidized loans to agriculture and export industries still carried fixed interest rates of 45% and 40%, respectively. Although these rates were increased last year, such loans have been fully adjusted for inflation only since the beginning of 1984, and they still are subsidized insofar as the real rate of interest charged is 3% per annum versus market rates in excess of 20%. Other subsidies to exports remain, such as income tax exemptions, excise tax credits, and accelerated depreciation allowances. Fuel price subsidies were not abolished until mid-1983, instead of at the beginning of that year. A wheat-import subsidy, of more than half the wholesale price, was to have been eliminated by June 1984 but, in fact, was not.

The biggest, and so far insurmountable obstacle to reducing the overall fiscal deficit is the servicing of the enormous cruzeiro-denominated debt of the Brazilian public sector — almost all of it indexed. This debt is the legacy of many years of

deficit spending by all levels of government and by public companies and agencies. Their spending was financed mostly through loans from the domestic banking system and the issuance of debt to the nonbank public. These stocks of domestic debt are adjusted for inflation, through the application of a monetary correction index, or in certain cases for currency devaluation. Consequently, the authorities cannot control the cost implicit in the debt's automatic revaluation — the more so as the monetary correction index now reflects inflation accurately. The budgetary cost of indexation can be reduced in real terms only if the public sector runs an operating surplus and uses it to retire debt. Until now, however, fiscal expenditures have outstripped revenues.

Last year, the overall deficit increased by 3% of GDP, from 16½% of GDP in 1982 to 19½%, instead of falling by the equivalent of 6% of GDP as originally planned. In 1984, the deficit may be cut to around 16% of GDP — marginally below the 1982 figure but far short of the 9% of GDP reduction that was hoped for at the beginning of last year. Thus, the fiscal imbalance and its financing remain the driving force of high inflation in Brazil.

The very slow fiscal progress inevitably has weakened the ability of the monetary authorities (the Banco Central do Brasil and the Banco do Brasil) to carry out a restrictive credit policy. Besides having to fund and even administer many programs entailing a subsidy, the authorities have had to lend financial support to an ailing social security system and cover the unpaid foreign obligations of some state enterprises.

A further impediment to monetary restraint is the existence of over $12 billion in dollar-indexed deposits at the central bank — about twice the size of the monetary base. These deposits were opened several years ago to capture the unutilized portion of the foreign borrowings of state-owned and private companies, including multinationals. A rise in cruzeiro interest rates would encourage companies to draw on these so-called Resolution 432 deposits and to liquidate local-currency debts. The resulting increase in the monetary base, much the same as a capital inflow, could substantially offset the central bank's restrictive stance.

The failure of monetary restraint is evident on several counts: the persistent acceleration in growth of the monetary aggregates; the behavior of inflation itself; and interest rates that are not convincingly positive in real terms. The monetary base and M1, targeted at 60%, increased by about 90% in 1983, while M3 rose 170%. By last month, the monetary base and M1 were up 100% and 112%, respectively, from a year earlier rather than the intended 70%. And the broader monetary aggregates increased by over 200% (see Chart 4).

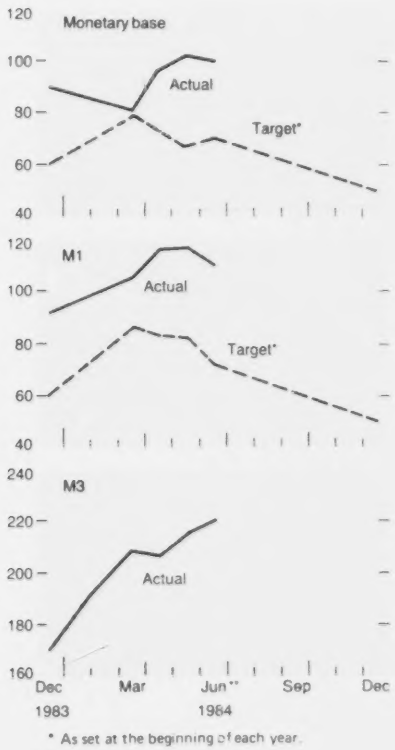
The rate of inflation, which initially was meant to fall well below 100%, actually jumped to 211% in 1983 as measured by the general price index. It has remained above 225% in the past several months, with no evident downward trend.

As for interest rates, on the surface they now appear strongly positive in real terms, at least since late 1983 when monetary correction was reformed to reflect inflation fully. Commercial bank CD rates are on the order of 20% per annum in addition to monetary correction, and lending rates are higher still. However, given past practices, lenders and borrowers can hardly be confident that monetary correction will continue to compensate for actual inflation, let alone in after-tax terms. Thus, it is by no means clear that interest rate policies are signaling monetary restraint. Even so, the cen-

Chart 4

Monetary aggregates

percent change from previous twelve months



* As set at the beginning of each year.

** May and June estimated.

tral bank displays concern that truly high real interest rates would crowd out the private sector's credit needs and plunge the economy into severe recession. Moreover, a sharp rise in interest rates could endanger the financial system: recession and the fall in real wages already have led to a growing wave of payments arrears on the part of mortgage borrowers and home builders.

Outlook

Barring any major policy initiatives during the months to come, the new Brazilian government that takes office on March 15, 1985 following selection of a new president is likely to inherit an economy characterized by very high inflation, low economic growth, and an improved current account and international reserves situation. The new administration probably will seek to change this economic configuration. There certainly will be pressure from all groups in society for an early return to higher rates of economic growth. The resumption of growth, however, requires stepped-up saving.

Significant reliance on foreign finance at this stage is neither possible nor desirable. The indebtedness built up over the years is already heavy. Brazil's total foreign debt is about to reach $100 billion, three-and-a-half times the value of annual exports of goods and services. Interest payments of about $12½ billion this year amount to more than 40% of export earnings. There is an urgent need to reduce the relative size of this debt burden, both by slowing the growth of debt and further boosting the growth of exports — objectives consistent with prevailing conditions in international capital markets, which require countries to prove their ability to generate foreign exchange and keep debt growth to a minimum.

If the Brazilian economy is to grow in real terms by 4%-6% per annum on a sustainable basis while avoiding balance of payments difficulties, the incoming administration must tackle above all the fiscal problem. The public sector's absorption of nearly all private and foreign savings has to be diminished steadily by at least 2%-3% of GDP per year so that resources can be released to underwrite economic expansion. This release of resources does not guarantee that economic expansion will take place unless the private sector is willing to put those resources to work. In the case of Brazil, however, the private sector has demonstrated impressive dynamism even under the difficult circumstances of the past few years. Thus, there is ample reason to expect that it can move ahead given new resources and correct market signals.

The most meaningful fiscal reform can be made in the screening and financing of public-sector investment activities. In Brazil in the 1970s public enterprises were created for specific projects — often, some of the most ambitious and expensive in the world, such as hydroelectric dams, nuclear plants, subway systems, rail lines, and mining and industrial ventures. These projects, usually requiring five or more years to carry out, were justified on the basis of extrapolations of future demand for energy, transportation, steel, and the like. But the newly created companies had no immediate cash-generation ability of their own.

A different pattern is warranted for the future. A national priority list could be drawn up with World Bank assistance establishing which are the most worthwhile projects closest to completion. These are the projects that merit continued funding, in preference to others that may indeed be viable but whose payoff is less certain or immediate. Until most of the projects under construction

Table 7

Balance of payments

annual average percent charges, except as noted

	1984	1985	Average 1986-90
Assumptions			
OECD real GNP	4.0	2.8	2.3
*OECD inflation**	0.0	8.0	6.0
LIBOR, % per annum	12.0	12.0	9.0
OPEC oil prices	—2.0	—2.0	6.0
Brazil real GDP	0.5	3.0	5.4
Results			
Merchandise exports	14.0	9.0	9.6
Merchandise imports	—7.0	7.5	13.1
Non-oil imports	9.0	17.0	16.0
Trade surplus, $ billions	10.5	11.7	13.2
Interest payments, $ billions	—12.6	—13.8	—11.7
Current account, $ billions	—5.1	—4.5	—3.0
External debt, $ billions			
at year-end	103	108	113**
% of total exports	355	340	235**

*Manufactures prices in dollar terms.
**1990.

are finished, new projects should be eschewed. Moreover, financing needs for all projects should be met, to a much greater extent than hitherto, through internal cash generation: operating concerns must increase prices substantially above break-even levels and thereby contribute to other public-sector companies — those that have no current revenues and that must therefore borrow to finance profitable investments. A second avenue to raise funds should be the sale of equity participations, whether through the stock exchange (as done to a limited extent by Petrobras, CVRD, and the Banco do Brasil) or by way of joint ventures with local and foreign capital (Usiminas, Cobra, and Siderurgica de Tubarao). The combination of a short list of priority projects and minimal reliance on debt issuance could appreciably diminish public-sector borrowing.

Substantial savings can be obtained by the continued elimination of subsidies. Aside from phasing out those to wheat consumption and sugar production, as was pledged a year-and-a-half ago, the authorities should review other subsidies. Principal among them are the tax and credit benefits accorded to companies exporting manufactured goods — instituted when neither the cruzeiro nor labor costs were as competitive as they are now. If, as is sometimes argued, they are still needed to compensate exporters for the cost of high tariffs and other import restrictions, industry ought to avail itself of the drawback scheme that has been expanded recently thanks to World Bank funding. This scheme enables exporting companies to import necessary raw materials, parts, and components duty-free. Unlike most subsidies now available to exporters, this program is more acceptable internationally and is thus less susceptible to countervailing duties.

As for the social security system, it has not been possible to cover its ballooning expenditures through higher contributions or indirect taxes. Ever-increasing transfers from the treasury and loans from the central bank have proved necessary. The basic problem is that eligibility requirements are too liberal, for example, granting retirement benefits after at most 35 years of work, regardless of age. A recent survey showed that 60% of those receiving pensions had started to collect by age 55 — and could expect to continue to do so for about 20 more years. Even mature industrial countries with far greater per capita incomes than Brazil find such liberality of social provision burdensome.

Neither increases in tax rates nor reductions in wages offer much further promise. The country's tax burden has increased substantially in recent years and is quite high by international standards. Although the revenue yield has been less than anticipated, it will rise over time once the pace of economic activity recuperates. Moreover, the collection problem will ease as inflation abates. The current wage policy probably has delivered all the expenditure savings it can wisely attempt. In fact, if the legislation is not soon amended, public-sector efficiency will suffer: the best-qualified civil servants and the skilled workers and managers of state enterprises — those who have suffered a major erosion of their standard of living — will leave their jobs in the public sector. More enlightened wage legislation would allow free collective bargaining in the private sector; give management in state enterprises the right to set compensation levels in accordance with profitability; and grant other public-sector employees raises in line with inflation, including a partial catch-up for higher-paid civil servants.

Brazil also needs to address weak-

nesses in its financial system, notably the problems of its savings and loan institutions. The inability of those banks to earn enough on their portfolios to cover the interest they must pay to their depositors calls for fiscal assistance. It probably would entail limiting their mortgage lending to low-income borrowers to an amount covered by a budgetary allocation, and injecting additional capital. The objective ought to be to free the monetary authorities from the constraints arising from the weak condition of the savings and loan institutions.

Reduced reliance on foreign savings is not only dictated by international debt considerations, but also is consistent with the favorable balance of payments outlook despite high dollar interest rates. Already Brazil has reduced its current account deficit by two-thirds since 1982, an improvement won not just by slashing imports but also, and increasingly, through export expansion. Although the pace of economic growth in the industrial countries will presumably slow from the rapid 4% or more now projected for 1984, Brazil's goods and services exports can reasonably be expected to rise at an annual average rate of about 10% during the second half of the 1980s (see Table 7). To be sure, Brazil's exports would be set back by any new slowdown in OECD activity, such as will very likely occur at some point. However, even on a conservative assessment it seems realistic to envisage Brazil's trade surplus edging higher from the present level of $10-$12 billion to perhaps $15 billion by the end of the decade. This would shrink the current account deficit to about $3 billion per annum on average, and quite possibly less at least in some years. On the same reading, the critical foreign debt to exports ratio could decline from its present 350% to below 250% by the end of the decade, perhaps even close to 200%.

With the current account deficit so much reduced, Brazil's needs for fresh commercial bank credit should run to only $2-$3 billion per annum in 1985-87, and could be even less thereafter. Thus, during the next three years creditor bank exposure would rise barely 3% annually, well below both the recent and prospective growth of the banks' capital. Most of this new bank money could be provided through cofinancings with the World Bank; the possibilities are now being explored by the Brazilian authorities. Despite these small new money requirements, it would still be constructive for Brazil and its creditors to restructure maturities on the country's outstanding obligations. If such restructuring provides an appropriate grace period, it will be possible to bring down Brazil's gross financing requirements during the remainder of the decade to a level not much greater than its net new money needs.

All this adds up to a rather favorable outlook for Brazil's balance of payments and financing. Even more significant, it is achievable in conjunction with a return to economic growth in Brazil of at least 5% per annum. There is a further avenue by which Brazil can advance its growth prospects, while still holding down the growth of foreign debt. Brazil has the potential to attract significant foreign savings through a more hospitable approach to overseas direct investment. This would entail a relaxation of existing restrictions which place the country at a disadvantage relative to other developing and industrial countries. Not only would increased private foreign investment inflows help the balance of payments, they also would confer important benefits in new technology — an area in which Brazil cannot afford a go-it-alone approach. With good export-oriented management, the coupling of both foreign and indigenous technology with the country's unequaled natural resource endowment can once again set Brazil on the road to healthy economic growth and rising living standards.

Statistical appendix

for key to data in tables see April 1984 issue.

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Information herein is from sources considered to be reliable but is furnished without responsibility on the part of Morgan Guaranty Trust Company.

Nominal effective exchange rates

Index numbers, 1980-82 average=100. Each index shows a currency's trade-weighted appreciation or depreciation measured against 15 other major currencies, using averages of daily noon spot exchange rates in New York and bilateral trade weights based on 1980 trade in manufactures. Annual figures are calendar year averages.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Neth-erlands	Spain	Swit-zerland	Den-mark	Norway	Swe-den
Pre-June 1970 parities	114.6	114.4	69.0	116.4	111.1	66.2	226.2	147.5	80.6	91.1	82.1	143.2	51.3	113.0	92.3	119.6
Smithsonian central rates	103.1	121.9	77.2	116.7	109.8	68.9	220.9	146.7	80.6	92.3	82.9	142.7	53.2	110.8	90.9	117.6
1980	90.7	100.4	95.5	96.0	106.5	100.0	108.4	99.8	99.4	105.9	100.2	106.5	95.4	105.1	98.2	103.9
1981	99.5	100.2	105.8	104.0	100.4	97.2	98.8	102.1	98.9	101.8	97.1	99.4	98.3	99.2	100.1	103.3
1982	109.8	99.4	98.6	100.1	93.1	102.8	92.8	98.1	101.7	92.3	102.7	94.1	106.3	95.7	101.7	92.8
1983	114.2	100.8	107.8	92.0	87.3	107.6	90.3	91.6	103.6	90.0	105.0	78.4	111.5	96.4	99.4	82.2
1983																
July	115.1	101.0	106.9	89.8	86.2	107.2	90.6	93.4	103.5	89.7	104.5	76.8	111.7	95.4	99.9	82.6
August	117.0	101.2	106.2	91.5	85.6	106.5	89.6	94.0	103.1	89.2	104.1	77.0	112.3	94.5	100.3	82.8
September	116.7	101.3	107.1	92.2	85.6	106.9	88.9	93.8	103.3	88.8	104.2	76.7	112.4	94.9	100.9	82.6
October	114.8	101.0	110.7	93.5	85.4	108.0	88.6	92.2	103.8	88.7	105.0	76.0	113.2	95.2	100.8	82.3
November	116.5	100.9	110.7	94.8	85.1	107.1	88.3	92.8	103.2	88.4	104.4	75.9	112.8	94.6	100.9	82.7
December	118.0	100.4	112.1	94.2	84.7	106.8	88.0	91.8	102.8	88.2	104.1	75.8	113.8	94.0	99.5	83.1
1984																
January	119.1	100.5	113.3	95.5	84.1	106.5	87.6	91.5	102.6	87.7	103.7	76.3	113.8	93.6	99.2	83.4
February	117.3	100.2	111.9	97.3	84.7	108.0	87.0	91.4	103.5	88.3	104.3	77.1	112.2	94.0	99.0	82.9
March	115.4	98.0	114.7	97.2	85.3	109.0	87.2	89.8	104.2	89.0	105.0	77.2	111.7	94.6	98.7	83.5
April	116.7	97.5	115.7	95.1	85.2	108.6	87.3	88.9	104.1	89.0	104.8	78.1	111.3	94.0	98.9	83.7
May	119.5	96.8	114.6	95.1	84.6	107.7	86.9	89.1	103.8	88.8	104.4	78.4	110.9	93.6	99.1	83.6
June	120.2	96.2	113.3	93.0	84.9	108.2	87.0	88.6	104.2	88.9	104.6	78.0	110.1	93.8	99.1	83.4
June 1	119.2	96.8	114.0	94.1	84.9	108.2	87.0	88.9	103.8	88.8	104.5	78.2	110.9	93.6	99.1	83.3
8	118.7	96.3	113.9	93.9	85.1	108.6	86.9	88.6	104.5	89.1	104.8	78.4	110.5	94.0	99.2	83.1
15	119.6	96.3	113.6	93.9	84.9	108.2	87.0	88.7	104.5	89.0	104.6	78.3	110.0	94.1	99.4	83.4
22	120.7	96.4	113.4	92.8	84.7	107.8	87.0	88.8	104.1	88.9	104.4	77.9	110.1	93.7	99.5	83.6
29	122.0	95.7	112.3	91.4	84.7	107.8	87.2	88.3	104.0	88.9	104.4	77.6	109.6	93.6	98.5	83.9
July 6	123.5	95.4	110.3	91.7	84.7	107.7	87.5	87.7	104.3	89.2	104.3	77.5	109.0	93.7	98.1	84.3
13	124.1	94.9	111.2	90.0	84.7	107.9	87.5	87.0	104.0	89.2	104.2	77.2	108.3	93.7	97.6	84.3

Real effective exchange rates

Index numbers, 1980-82 average=100. Each index is the corresponding nominal effective exchange rate adjusted for differential inflation in wholesale prices of nonfood manufactures. Underlying price data are partly estimated. Index revisions reflect revised price information or, less frequently, adoption of new price indices to measure inflation in one or more countries.

	United States	Canada	Japan	Australia	France	Germany	Italy	United Kingdom	Austria	Belgium	Neth-erlands	Spain	Swit-zerland	Den-mark	Norway	Swe-den
1980	89.4	99.6	103.0	93.0	102.1	103.5	103.5	99.8	100.2	107.4	99.9	101.9	98.7	103.6	96.6	101.2
1981	100.7	100.0	104.6	102.8	100.2	97.3	98.7	102.3	99.1	100.3	97.6	99.0	98.8	99.4	100.9	102.0
1982	109.9	100.4	92.3	104.3	97.7	99.2	97.8	97.9	100.7	92.3	102.5	99.1	102.6	97.1	102.5	96.7
1983	112.7	103.0	96.6	100.1	95.9	99.4	100.0	92.0	101.6	92.1	101.8	89.5	105.3	98.8	101.3	91.5
1983																
July	113.5	103.8	95.4	97.6	95.3	98.5	100.4	93.9	101.4	92.0	101.5	87.9	105.0	97.0	101.2	92.8
August	115.5	103.9	93.8	99.6	94.6	98.2	99.1	94.4	100.7	91.7	101.1	88.1	106.0	96.3	101.1	93.3
September	114.2	104.4	94.9	101.1	95.2	98.3	99.6	94.4	100.6	90.8	101.1	88.3	105.7	97.8	103.3	92.5
October	113.3	103.3	97.4	102.4	95.6	98.9	99.7	92.5	101.4	90.8	101.0	87.9	105.9	97.7	102.7	92.5
November	114.5	103.2	97.4	104.1	95.5	97.8	99.7	93.3	100.8	90.8	100.2	88.4	105.9	96.9	102.4	93.3
December	115.6	103.0	98.6	103.8	95.6	97.4	99.8	92.1	100.4	90.3	99.8	88.9	106.4	95.7	101.5	94.1
1984																
January	116.2	103.5	99.2	105.5	94.4	96.7	100.2	91.9	102.2	89.9	100.5	89.9	106.1	95.4	101.3	95.1
February	114.2	103.5	97.7	107.7	95.6	97.8	100.0	91.9	102.9	90.1	101.2	91.0	104.3	97.0	101.5	94.7
March	112.0	101.6	99.8	107.8	96.8	98.5	100.5	90.6	103.7	90.5	101.7	91.7	103.9	96.3	101.0	95.7
April	113.0	101.4	100.4	105.8	96.9	98.0	101.0	89.9	103.0	90.0	102.0	92.3	103.5	95.6	101.0	95.6
May	115.6	101.0	99.1	106.0	96.6	97.0	101.2	90.2	102.3	89.4	102.0	93.1	102.9	94.8	100.7	95.9
June	116.1	100.7	97.6	103.9	97.2	97.2	101.7	89.9	102.8	89.1	102.3	92.9	102.1	94.8	100.7	95.9